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into
Residential Tenancies

Overview of Alternative Rental Housing Policies

John Chant

Research Study No. 19

OVERVIEW OF ALTERNATIVE RENTAL HOUSING POLICIES

by

John Chant

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TABLE OF CONTENTS

PAGE

Chapter 1 Introduction

1.0 Policies in Perspective 1
1.1 The Choice Among Policies 2
1.2 Provincial Policy in a Federal State 4

2.0 Method of Analysis 7
2.1 The System of Classification 8
2.2 The Goals of Rental Housing: An Initial Perspective 8

3.0 The History and Evolution of Housing Policy in Ontario 11
3.1 The Goals of Housing Policy 13
3.2 The Instruments of Housing Policy 24

4.0 Policy Toward Ownership of Housing 26

5.0 Taxation and Housing Policy 30
5.1 Federal Tax Reform: 1971 30
5.2 Taxation and Housing Choice 32

6.0 Organization of the Study 37

Notes to Chapter 1 39

Appendix to Chapter 1: Description of Rental Housing Programs by Pearl Ing 41

Chapter 2 Classification of Rental Housing Policies

1.0 Introduction 85

2.0 Market and Non-market Allocation 85

3.0 Types of Housing Policies 88
3.1 Budgetary Versus Non-Budgetary Policies 90
3.2 The Workings of Market Augmenting Policies 92

4.0 Demand Augmenting Policies 95

5.0 Supply Augmenting Policies 96

6.0 Market Replacing Policies 98

7.0 Rent Regulating Policies 99

Chapter 2 (cont'd)

8.0 Institutional Policies 101
  8.1 The Purpose of Construction Standards and Land Use Controls 103
  8.2 The Costs of Construction Standards and Land Use Controls 103
  8.3 The Distribution of Costs and Benefits 104

9.0 The Classification in Action 107

Notes to Chapter 2 111

Chapter 3 Evaluation Criteria for Rental Housing Policies

1.0 Introduction 112

2.0 Framework for Policy Evaluation 113
  2.1 Constraints on Policy 114
  2.2 Other Dimensions of Evaluation Criteria 116

3.0 Affordable Housing 118

4.0 Adequacy of Income 120
  4.1 Horizontal Equity 120
  4.2 Vertical Equity 124
  4.3 Income as a Measure of Equity 124
  4.4 The Interpretation of Equity Effects 130
  4.5 Equity Effects of Individual Policies 133

5.0 Adequacy of Housing 134
  5.1 The Desirability of Housing Benefits 134
  5.2 The Externality Argument 139
  5.3 Special Needs 140
  5.4 What Is Special About Housing? 142
  5.5 The Interpretation of Housing Adequacy 143

6.0 Incidence of Cost 145

7.0 Effectiveness for Cost 147

8.0 Rent Gouging 149

9.0 Security of Tenure 152

10.0 Economic Efficiency 153
  10.1 Information and Transactions Costs ... 153
  10.2 Efficiency of Housing Use 156
  10.3 General Economic Efficiency 157

Chapter 3 (cont'd)

11.0 Diversity and Balance in Communities 158

12.0 Administrative Efficiency 160

13.0 Feasibility 163
  13.1 Level of Government 163
  13.2 Problems of Different Communities 165
  13.3 Political Considerations 166

14.0 Conclusions 168

Notes to Chapter 3 172

Chapter 4 Assessment of Demand Policies

1.0 Introduction 173

2.0 Housing Allowance Allocations 174

3.0 The Experimental Housing Allowance Program 178
  3.1 The Demand Experiment 179
  3.2 The Supply Experiment 181
  3.3 The Demand Supply Experiments Compared 182

4.0 Assessment of Unconstrained Housing Allowances 183
  4.1 An Unrestricted Housing Allowance 184
  4.2 The Workings of Unconstrained Demand Policies 185
  4.3 Adequacy of Income: Unconstrained Housing Allowance 190
  4.4 Adequacy of Housing: Unconstrained Housing Allowance 192
  4.5 Effectiveness for Cost of Unconstrained Housing Allowances 194

5.0 Assessment of Constrained Housing Allowances 195
  5.1 The Workings of a Rent Constrained Program 196
  5.2 Adequacy of Income: Rent Constraint 198
  5.3 Adequacy of Housing: Rent Constraint 201
  5.4 Effectiveness for Cost: Rent Constraint 203
  5.5 The Workings of Housing Allowances with Eligibility Constraints 204
  5.6 Adequacy of Income: Eligibility Constraint 206

Chapter 4 (cont'd)

5.7 Adequacy of Housing: Eligibility Constraint 212
5.8 Effectiveness for Cost: Eligibility Constraint 216

6.0 Housing Allowances and the Workings of the Rental Housing Market 218
6.1 Expectations of Full Programs 221

7.0 Rent Gouging 223

8.0 Security of Tenure 224

9.0 Economic Efficiency 225

10.0 Administrative Efficiency 228
10.1 Direct Costs 228
10.2 Indirect Costs of Administration 233
10.3 Flexibility 233

11.0 Community Needs 234

12.0 Feasibility 234
12.1 Level of Government 234
12.2 Cooperation Among Governments 235
12.3 Political Support 235

13.0 Scale of Costs 237

Notes to Chapter 4 243

Chapter 5 Assessment of Rental Housing Policies: Supply Policies

1.0 Introduction 245

2.0 The Workings of General Subsidy Programs 246
2.1 Who Benefits? 252
2.2 Cost of Subsidies 253

3.0 General Subsidies: Tax Incentives for Rental Housing 254
3.1 Depreciation Allowances 254
3.2 MURB's 256

4.0 Assessment of Tax Programs 260
4.1 The Workings of Tax Incentives 260
4.2 Absence of Tax Incentives 265

5.0 Affordable Housing 271
5.1 Adequacy of Income 271
5.2 Adequacy of Housing 278

6.0 Effectiveness for Cost 283
6.1 Adequacy of Income 283

Chapter 5 (cont'd)

6.2 Adequacy of Housing 285

7.0 Economic Efficiency 286

8.0 Administrative Efficiency 286

9.0 Feasibility 287

10.0 Cost Estimates of the MURB Program 288

11.0 Directed Subsidies 290

12.0 The Workings of Directed Subsidies 290
- 12.1 Who Benefits? 293
- 12.2 The Assessment of Directed Subsidies 294

13.0 Effectiveness for Cost 295

14.0 Security of Tenure 297

15.0 Economic Efficiency 297

16.0 Administrative Cost 298

17.0 Feasibility 298

Notes to Chapter 5 301

Appendix to Chapter 5: MURB Cost Estimates 303

Chapter 6 Assessment of Rental Housing Policies: Market Replacing

1.0 Introduction 314

2.0 History of Public Housing 315

3.0 The Workings of Public Housing Programs 316

4.0 Affordable Housing 320
- 4.1 Adequacy of Income 320
- 4.2 Adequacy of Housing 332

5.0 Effectiveness for Cost 333
- 5.1 Adequacy of Income 333
- 5.2 Comparative Expense 337
- 5.3 Administrative Expense 340
- 5.4 Adequacy of Housing 341

6.0 Rent Gouging 342

7.0 Security of Tenure 343

Chapter 6 (cont'd)

8.0 Economic Efficiency 343

9.0 Administrative Efficiency 346
9.1 Flexibility 346

10.0 Feasibility 347
10.1 Level of Government 347
10.2 Adaptability to Community Needs 348
10.3 Basis for Political Support 349

11.0 Conclusions: Public Housing 351

12.0 Introduction: Non-Profit Housing 351

13.0 Objectives of Non-Profit Housing 352

14.0 The History and Development of Non-Profit Housing 354
14.1 The Extent of Non-Profit Housing 356

15.0 Assessment of Non-Profit Housing Programs ... 357

16.0 Who Has the Equity? 358
16.1 Who Has the Benefits? 358

17.0 Effectiveness for Cost 361

18.0 Security of Tenure 363

19.0 Economic Efficiency 363

20.0 Income Mix 364

21.0 Conclusion: Non-Profit Housing 370

Notes to Chapter 6 372

Chapter 7 A Comparison of the Alternatives

1.0 Introduction 373

2.0 The Method 374
2.1 Definition of Equivalent Base 374
2.2 The Programs to be Examined 376
2.3 Target Households 377
2.4 Participation Rates of Eligible Households 379

3.0 The Effects of Unconstrained Demand Assistance 382
3.1 The Assistance Formula 382
3.2 Assistance per Participating Household 383

Chapter 7 (cont'd)

3.3 Increased Housing Expenditure per Participating Household 387
3.4 Increased Housing Consumption 388
3.5 Summary of Unconstrained Demand Program 391

4.0 Constrained Demand-Side Assistance 391
4.1 The Assistance Formula 391
4.2 Assistance per Participating Household 392
4.3 Increased Housing Expenditure per Participating Household 394
4.4 Increased Housing Consumption 398
4.5 Summary of Constrained Demand Program 402

5.0 Subsidized Supply Program 403
5.1 Rent Supplement Program 1 403
5.2 Summary of Impact of Rent Supplement Program 407

6.0 Public Housing 407
6.1 The Program 407
6.2 Differences in Costs 409
6.3 Recipient Households 409
6.4 Value to Recipients 410
6.5 Increased Numbers of Rental Units 411
6.6 Summary of Impacts 412

7.0 Summary Comparisons 413
7.1 Eligibility of Households and Distribution of Assistance Among Them 413
7.2 Income Transfers to Low Income and Other Households 415
7.3 Increased Housing Consumption 418

Notes to Chapter 7 422

Appendix 1 to Chapter 7: The Elasticity of Supply of Rental Housing 424

Appendix 2 to Chapter 7: Estimates of the Costs of a Constrained Housing Allowance: The Effects of Income Dispersion 435

Chapter 8 Conclusions

1.0 The Role of Complementary Policies 441

2.0 The Interrelation Between Budgetary and Non-budgetary Policy 441

3.0 The Performance of Complementary Policies ... 443

4.0 The Performance of Rent Control 447

Chapter 8 (cont'd)

5.0 The Choice of Policy in Perspective 451
Note to Chapter 8 454

Bibliography 455

CHAPTER 1: INTRODUCTION

1.0 Policies in Perspective

The Commission of Inquiry into Residential Tenancies was created by the Province of Ontario with terms of reference which include:

> 1. to examine, study and inquire into the laws of Ontario, including the statutes and regulations passed thereunder affecting residential tenancies in Ontario for the purpose of determining,
>   a) the equity of the current system of rent review, having regard for the rights and interests of both the landlord and the tenants;
>   b) the effect of rent review on the level of rental rates and the supply of residential accommodation in the province;
>   c) whether a more expeditious procedure should be applied to the review and decision-making process of the Residential Tenancy Commission in view of the issues being raised, the right of appeal and the need for timely decisions;...

To achieve these ends, the Commission has undertaken a series of studies examining rent regulation and its ability to contribute to achieving the goals which have been proposed for rental housing policy.

Unlike other studies in the series, the present one does not focus on rent regulation itself. Rather, it derives from the Commission's further mandate

> to recommend what measures, in addition to rent review, the Province of Ontario might take to assist in providing rental accommodation at fair rents.

Thus, this paper assesses the relative merits of other types of policies by which the government can influence the rental housing market in attaining the goals of housing policy.

1.1 The Choice Among Policies

In formulating housing policy, government policy makers are faced with a wide range of possible instruments that they can use.(1) Each instrument of housing policy has different effects on the various goals of housing policy. One instrument will be unlikely to dominate all others in every dimension. An instrument may have an advantage with respect to some goals toward which it contributes more effectively than other instruments. It may still contribute less effectively but still positively with respect to other goals. Finally, an instrument may have undesirable side-effects in that its use may be positively detrimental to the achievement of other goals.

The differential impacts of different instruments on the various goals of policy have a number of important implications. The exclusive use of a single instrument is not likely to be the best approach to the achievement of policy goals, overall. Such an approach could be appropriate if policy were just an exercise directed at only one goal without any consideration of any other. Then the instrument which is most effective for achieving that goal would be chosen as the sole means of policy. The formulation of policy, however, reflects not just the choice of one goal but rather the choice among a multitude of goals which results from the trading-off of a variety of interests. As a result, policy makers must choose a package of instruments which best contributes to the attainment of their goals.

The choice of a combination of instruments also means that the effects of a single instrument cannot be considered solely with respect to only one goal because its effects in other dimensions are germane to the overall performance of policy. Moreover, the performance of an instrument cannot be judged in isolation of other instruments which affect the same objectives. An instrument must be judged in terms of its contribution to the performance of the best package of instruments available for achieving the objectives of policy. It is quite possible, considered in isolation, that an instrument ranks high in terms of its contribution toward an important goal, but may not be part of a comprehensive program of policies because combinations of other instruments match its performance without any detrimental side-effects.

A final factor which must be taken into account is the fact that every policy has widespread effects beyond its intended area of influence. Tariff policy, for example, has an impact on labour markets, on the volume of foreign investment and income distribution, among other things. So too, it is not possible to make a clear delineation of the set of policies which can be designated as rental housing policies. Thus, though rent regulation and the policies viewed in the study can be characterized as rental housing policies, it is more difficult to delineate where rental housing policies stop. Homeownership policies, in particular, also have an impact on rental markets. A policy which alters the cost of homeownership has a substitution effect. If homeownership becomes relatively cheaper, households will be induced to shift from rental housing toward homeownership. Housing policies also work through the supply side of the market. Owner-occupied houses and rental units, for example, compete for the same land. More directly, either ownership or rental policies may encourage the conversion of rental units into condominiums, reducing the supply of rental housing and increasing the supply of ownership units.

The general argument presented above must be taken into account in any review of any housing policy. A review of rent regulation as a component of housing policy must extend to compare rent regulation with other approaches to the same goals and to examine the interactions of rent regulation with these other policies. These other policies may attain certain goals of housing policy more effectively than rent regulation. Such a finding would indicate that the emphasis of rent regulation and other policies must be directed toward those goals for which they have a relative advantage. Alternatively, other policies may be capable of overcoming side-effects with respect to some goals that may result from using rent regulation in the pursuit of any goals for which it may be suited.

1.2 Provincial Policy in a Federal State

The preceding discussion of the choice among policies has proceeded from the assumption that the policy maker is able to implement those instruments of policy which are best for the present purpose and refuse to use those that fail to contribute to or even hamper the attainment of the goals of policy. Such an approach would be appropriate for a unitary state when only one level of government conducts policy.

This analysis would be a misleading characterization of policy for a government in a federal state which must recognize and take into account the policies of other levels of government in formulating its own.

The government of Ontario must take into account the actions of other levels of government in formulating its own policies regarding the central housing market. Like many constitutional issues, it is not clear with which level of government lies the ultimate authority for housing policy in Canada. Goldberg (1983) observes that Section 92 of the British North America Act assigns to provincial legislatures "exclusive responsibility for all matters of a merely local or private nature in the province" (p. 59), which includes municipal institutions and property and civil rights. At the same time, however, he notes that many federal responsibilities under Section 91 can influence housing markets. These powers include: regulation of trade and commerce 91(2); currency and coinage 91(14); banking, incorporation of banks, and the issue of paper money 91(15); and interest 91(19).

Municipal governments derive their powers from the provinces themselves under the provincial responsibility for municipal institutions. Goldberg argues:

> Provincial governments, in turn, have delegated to municipalities the powers to regulate land use and subdivision activity, and to control the type of urban development within each municipality. (p. 60)

The de facto responsibility for actual rental housing policies may differ from the constitutional assignment of powers. In fact, as the review in Section 3.0 below shows, until recently the history of housing policy has been, first, a history of federal initiatives; then federal initiatives with provincial responses and only more recently, independent provincial initiatives. In many ways, the leadership of the federal govenment in housing policy is quite understandable. Early housing policy was directed toward general objectives such as maintaining activity in the construction industry and the alleviation of general housing shortages so that aggregate policies such as loan programs, guarantees and general subsidies were appropriate instruments. The federal government also commanded, to a greater degree, the financial resources which made such policies possible. Only as the goal shifted from such general goals to the redistributive goal of directing support to target households was the federal government required to seek the collaboration of the provinces to any substantial degree. The federal-provincial partnerships were developed as a means, first, to provide assistance to low income households through public housing.

The final shift in emphasis came with the implementation of rent regulation in 1975. Still, some tie persisted with the federal government, for the formal initiation of rent regulation in Ontario coincided with the anti-inflation program announced by the federal government. Nevertheless, the design and operation of rent regulation has been solely within the hands of the provincial government. Moreover, with the retreat of the federal government from participation in shared-cost programs, alleviation of the side-effects of rent regulation also appears to have become the responsibility of provincial governments, if only by default.

The provincial government cannot make its choice of policies independently of the actions of the municipal and federal governments. Policies differ with respect to the need for the cooperation of municipal governments for their implementation. Ideal policies in all other dimensions must be rejected if the municipal cooperation that is required for effective implementation will not be forthcoming. The policies of the federal government, however, are likely to be a greater constraint on choice by provincial governments. In the past, the federal-provincial partnership has involved the federal government in setting the terms under which provinces can qualify for financial assistance. Under such circumstances the provincial choice should no longer be among policies on the basis of the merits, ceteris paribus. One thing has not been kept equal, given the federal policies, and that is the cost to the province. From a purely provincial standpoint, the provincial government should consider policies on their merit, given their costs after federal assistance is taken into account.

2.0 Method of Analysis

The number and complexity of housing programs which have been used in or proposed for Ontario makes any comprehensive analysis on a program by program basis impossible. The appendix to this chapter gives some idea of this complexity by summarizing the essential features of present and past federal and provincial programs which have been directed toward the rental housing market. The multitude of different programs and their variants make it too easy to become lost in the details of programs without gaining any overall perspective of the workings of housing policies. Therefore, it has been essential to group policies into general types in which policies are classified according to the mechanism through which they influence the rental housing market.

2.1 System of Classification

The system of classification used in this study is developed in Chapter 3. It groups policies according to their initial impact on the rental housing market. The three types of policy identified are i) demand augmenting, ii) supply augmenting and iii) market replacing policies. Within each category, a few policies, actual or proposed, are taken as representative of that group of policies and analyzed in some detail. Each of these policies has a similar general purpose: alteration of the working of the rental housing for the purpose of attaining various social goals. The classification shows the way in which policies, which are directed toward the same general objectives, can work through different mechanisms in attaining these goals. The classification also can be used to assess the likely effects of proposed policies. Much can be learned about the effects of proposed policies from examining the characteristics that they share with past or existing policies.

2.2 The Goals of Rental Housing Policy: An Initial Perspective

Rental housing policies, as outlined in Section 3.0 of this chapter, have been directed toward a variety of goals with the overall emphasis changing over time. As a result, the present analysis cannot assess rental housing policies in terms of a single objective. Rather, the analysis proceeds by assessing each type of housing policy in terms of a range of criteria relevant to policy makers.

These criteria are derived, in part, from those developed by Stanbury (1984a) to assess the workings of rent regulation in Ontario. The use of common criteria is necessary inasmuch as rent regulation and the housing policies described in this paper are complementary methods for achieving the objectives put forward by policy makers for housing policy. Some additional criteria and further dimensions of criteria are considered in this study because of the special characteristics of the policies under review. The policies considered here are budgetary policies requiring the expenditure of government resources whereas the policies studied by Stanbury are regulatory policies intended to influence the behaviour of market participants without any direct expenditures of government resources.

The criteria used in this study are discussed fully in Chapter 3 below. By way of introduction, they can be summarized as follows:

1) Affordability of housing. This objective measures the degree to which rental housing policy can serve to make rental accommodation more affordable to lower income groups which are identified as the targets of housing policy. The affordability of housing depends on the interaction of prevailing rents with the incomes of target groups. Thus, this objective has been divided into two components for the purpose of the present study:

    a) Adequacy of income. This criterion measures the effects of different policies on the incomes of target households,
    b) Adequacy of housing. This second dimension of affordability measures the effects of policies on the supply of rental housing available at rents affordable to the target group of households.
2) Effectiveness for cost: Effectiveness of cost captures the degree to which a policy meets its affordability objectives efficiently. From the perspective of adequacy of income, it asks whether there are significant spill-overs beyond the target group, whereas from the perspective of adequacy of housing, it asks whether there are slippages between the distribution of assistance and increases in the availability of housing for target groups.
3) Rent gouging. This criterion assesses the degree to which a policy discourages rent gouging or ameliorates its effects.
4) Security of tenure. Security of tenure indicates whether a policy influences the tenure of target households. It includes the economic aspects of security of tenure and, in addition, any need to change residence in order to qualify for benefits.
5) Economic efficiency: This criterion measures the extent to which a policy creates incentives for efficient use of the stock of housing. It also considers the effects of policies on the efficient use of other resources, most especially, labour through its effects on labour mobility.

6) Administrative efficiency. Administrative efficiency refers to the additional costs incurred by the government itself, together with the costs imposed on the private sector, which arise from the implementation of the program. Assessment of this criterion requires examination of the administrative apparatus required to manage the program.

7) Feasibility. Feasibility reflects those considerations beyond those already discussed, which influence the probability that any type of policy would be implemented. It includes the appropriateness of the policy to the level of government concerned, the need for cooperation among governments and the degree to which the features of the policy can mobilize support in its favour from the various interest groups such as tenants, landlords, developers and taxpayers which may be identified with housing policy.

3.0 The History and Evolution of Housing Policy in Ontario(2)

Housing policy in Ontario can be traced as far back as 1919 when the federal government initiated a $25 million loan fund for provinces to assist municipalities in the construction of modest quality housing. The purpose of the project:

> Was not to provide housing for any particular group but to relieve what was thought to be a general scarcity of housing for Canadians. (Task Force on CMHC 1979, p. 5)

Fallis (1980) judges housing policy in Ontario:

> It is sometimes alleged that there is not now and never has been a "housing policy" in Ontario, only a series of improvised, often contradictory,

> responses to pressure of the moment. In the sense of a clearly enunciated blueprint actively implemented by various levels of government acting in concert, that is true. (Fallis, 1980, p. 12)

Fallis continues and observes correctly:

> However, that is a rather severe definition of policy. Using the simple criterion that "policy is what government does" one can discern in the legislation, administration and expenditures of governments, the housing policy in Ontario. (Fallis, p. 12)

The purpose of this section is not to provide a detailed documentation of the housing policies followed in Ontario. Rather, attention will be directed towards the changing goals of housing policy so as to illustrate the point that there is not one single criteria by which the effectiveness of housing policy can be judged. Instead, housing policy has been used as a means to attain a variety of goals over time and even at any one time, it may be directed towards several goals with unclear emphasis among them. In addition, this summary attempts to document the pervasiveness of government intervention in the housing market. This degree of government involvement has several consequences. Major changes in housing policy affect parties such as landlords, tenants and developers in fundamental ways. People have come to expect elements of housing policy and depend on them to the degree that they have made plans and decisions based on it. The direction of government policy is more than a minor determinant of their well-being. As a result, proposals for change take place in a hotly contested battleground and, as a consequence, must reflect an awareness of the interests of competing parties. In addition, any policy initiative must be undertaken only with an awareness of its interaction with already existing policies. A policy may have very different *effects when applied to a market otherwise unaffected by* government intervention than in a market shaped predominantly by government policies.

3.1 The Goals of Housing Policy

Housing policy in Canada has come a long way since the time one analyst could observe, "In Canada, housing as a political subject has, not to date, been a controversial one" (Wilson, p. 214). This statement need only be changed by one word -- the omission of "not" -- to describe the prominence of housing policy as a political issue in the 1970's and 1980's. Part of the reason for the politicization of housing has been the result of a transition of housing policy from being a means of stimulating economic activity through residential construction to being a major instrument of social policy for income redistribution.

Previous assessors of housing policy in Canada and Ontario have identified distinct phases of policy with respect to the objectives being pursued. The Task Force on CMHC (1979), for example, states:

> Throughout this period, housing has been used, when thought necessary, as an economic stimulation tool. However, the thrust of federal and provincial policies has shifted considerably, beginning with the emphasis in the thirties and forties on employment and demand stimulation, shifting in the fifties to a concern with the availability of housing finance and in the late sixties and most of the seventies to a preoccupation with social policy and income redistribution.... (p. 11)

A similar taxonomy of housing policy is presented by Fallis (1980):

> Ontario housing policy in the post-war period can be divided into three eras: 1945 to 1964, 1965 to 1975, and 1976 to the present. Although, of course somewhat arbitrary, because programs in one period continue into another and legislation enacted in one year may not produce significant results until later, this division does bring some order to the plethora of programs. (p. 12)

Both the Task Force and Fallis were commenting upon housing policies in general. Some indication of the changing goals of rental housing policy can be gained from examining major policy initiatives of the federal government presented in Table 1.1.(3)

The major policy initiatives taken, from the Provincial-Municipal Loan of 1919 until 1964 appear to reflect a concern with two issues: stimulation of the economy and alleviation of actual and potential scarcity of housing. Moreover, the emphasis, as far as housing was concerned, was directed toward owned rather than rental housing. The only major initiatives that reflect a concern with social housing were the National Housing Act of 1938 and the federal-provincial partnership for public housing in 1949. Wilson (1959) however, reports that:

> No units were produced under the legislation because of provincial delays in enacting necessary complementary legislation and because of wartime economic conditions. (p. 220)

TABLE 1.1

Major Initiatives in Rental Housing Policy

Date	Policy Initiative	Apparent Goals
1919	Provincial-Municipal Loan Program $25 million loans available to provinces	- alleviate scarcity of housing (Task Force, p. 5)
1935	Dominion Housing Act - $10 million loan fund for builders and owners - interest subsidy - capital guarantee - 75/25 loans	- stimulate economy (Task Force, p. 5)
1938	National Housing Act - 90/10 loans - subsidized loans for limited dividend companies, local housing authorities and non-profit associations, for low income rental projects - property tax relief	- reduce unemployment - improve housing conditions for families with low incomes (Task Force, pp. 5-6)
1944	National Housing Act - consolidation of previous programs - guarantee to suppliers of rental housing	- alleviate expected housing shortage - reduce unemployment
1946	CMHC created	- stimulate private production (Dennis-Fish, p. 129)
1949	Federal-provincial partership in public housing - federal government provides 75 percent capital and operating costs of public housing to provinces and through them to municipalities	- "provide much needed public housing" (Wilson, p. 221)
1954	National Housing Act - mortgage insurance - chartered bank lending power under N.H.A. - guarantee for loans	

TABLE 1.1 (cont'd)

Date	Policy Initiative	Apparent Goals
1964	Changed federal-provincial partnership - federal government provides 90 percent of capital cost and 50 percent operating subsidy for provincially or locally owned and operated public housing. Tenants pay 25 percent of income as rent - establishment of Ontario Housing Corporation (OHC) - loans to non profit housing	"Shifted focus of CMHC from one of market efficiency to one of redistribution" (Task Force, p. 8)
1967	- market determinator of interest rate for NHA insured loans - minimum term for mortgages reduced from 25 to 5 years - chartered banks permitted to make conventional mortgages	
1969	Rent supplement program covers difference between market rent and 25 percent of income	"targetted to low-income households residing in private private rental accommodation" (Government of Canada, 1985, p. 8)
1973	Non-profit and co-operation programs to give 100% loans to non-profit organization (charitable, provincial or municipal) and co-operatives to provide moderate and low income housing	"One of first federal low income programs which did not require matching subsidies from other levels of government" (Government of Canada, 1985, p. 8) "to provide housing for low and moderate income householders unable to locate or afford such housing on the open market... Priorities for funding were first,

Table 1.1 (cont'd)

Date	Policy Initiative	Apparent Goals
1973 (cont'd)		families of low and moderate income, with a high priority to areas needing new construction; Second, senior citizens and third special needs such as handicapped" (Government of Canada, 1985, p. 7).
1975	Implementation of Non-Profit and Co-operative programs in provinces where federal/provincial master agreements had been signed. Subsidy equal to difference between rent and 25 percent of income. Cost shared equally between federal and provincial governments.	
1975	Assisted Rental Program provided interest free assistance loans to entrepreneurs for new rental accommodation financed by private lenders in order to bring rents down to market levels.	
1978	Nonprofit and co-operative housing program provides subsidy equal to difference between mortgage amortization cost at market rates and 2 percent and is first used to reduce cost to lower end of market rents and then to assist low income tenants	
1981	Canada Rental Supply Plan (CRSP) supplies 15 year interest free loans up to $7500 per rental unit constructed	

SOURCES:

Government of Canada, Consultation Paper on Housing (January, 1985).

TABLE 1.1, Sources (cont'd)

Task Force of Canada Mortgage and Housing Corporation, Report on Canada Mortgage and Housing Corporation (October, 1979).

Lawrence Smith, "Recent shifts in policies affecting housing in Canada" in M.A. Goldberg (ed.) Recent Perspectives in Urban Land Economics (1976).

George Fallis, Housing Programs and Income Distribution in Ontario (1980).

Michael Dennis and Susan Fish, Programs in Search of a Policy: Low Income Housing in Canada (1972).

Similarly, Dennis and Fish (1972) report that:

> We [in Canada] have had a social housing program, on paper at least, since 1949. In practice, a minimum of funds or effort were expended on social programs until [the 1970's]. (p. 126)

Fallis (1980) summarizes this phase of Canadian housing policy aptly:

> Canadian housing policy until 1964 was dominated by a desire to increase the volume of residential construction, especially of single-family housing (p. 13)... The philosophy of the day was "to assist the private sector...". (p. 15)

A major change in housing policy occurred with the revision of the National Housing Act of 1964 which has been described by Patterson (1977) as a "watershed". This revision:

> Authorized the Corporation to provide direct loans to the province for 90 percent of the capital cost of public housing projects and to share the operating loss on a 50-50 basis; to make a 90 percent loan for land acquisition and servicing of the project; to loan to non-profit corporations owned by a province or municipality for low rental projects; and to permit greater funding of urban renewal programs for a wider range of projects. (Task Force, 1979, p. 8)

The Ontario government responded in the same year by creating the Ontario Housing Corporation "which saw its mandate as the immediate production of low income housing units" (Dennis and Fish, 1972, p. 147).

The Task Force (1979) viewed these changes as having a number of effects:

> First, they resulted in decentralization of housing policy, with provincial housing corporations beginning to assume increased responsibility. Second, the amendments shift the focus of CMHC from one of

> market efficiency concerns to one of redistribution. Thus, CMHC in conjunction with the provinces began to undertake programs such as land assembly which before had been undertaken by the private sector. (Task Force, p. 9)

This change in emphasis did not initially represent any abandonment of previous objectives. As Fallis (1980) observes:

> In the early 1960's the approach of government began to change, not so much out of dissatisfaction with the previous system -- the insurance program remained and extensive residual lending continued until 1971 -- but because it was felt more could be achieved. Attention shifted from market failure to income issues, and governments became much more involved in the housing market. (p. 16)

While this judgement refers to Canadian housing policy as a whole, a similar judgement has been made for Ontario by Dennis and Fish (1972):

> While Ontario was far and away the provincial leader in the provision of low income housing, it should be remembered that the total effort in low income housing produced only a very small percentage of the total units provided during that period in Ontario. For example, the 6,100 units of public housing represented less than 1 percent of the total number of housing units produced in Ontario during the period. (p. 147)

Nevertheless, there is no doubt that the 1964 initiative represented a clear change of direction. The CMHC Task Force, for example, observed:

> By the late sixties, the changes in the objectives of federal and provincial housing policy were increasingly evident. For example, between 1949 and 1967, a nineteen year period, approximately $172 million was committed for public housing. In comparison, in the two years 1968 and 1969, over $377 million was committed to public housing. (1979, p. 9)

The nature of the change became further evident by 1967 when, as the Task Force observed:

> The federal government was faced with a difficult choice. Either it could withdraw substantially from the provision of direct loans to finance large volumes of "private market housing"; ignore the provincial demands for funds to finance social housing; or substantially increase its financial commitment to housing. (1979, p. 9)

Faced with this quandary, the federal government chose the second alternative of supporting provincial priorities while dealing with the finance of private housing by making residential mortgages more attractive to private lenders. Fallis (1980) summarizes the essence of this changed emphasis clearly:

> Housing was classed with education and health care as something to which everyone was entitled as a right. In the early 1970's the minister of state for urban affairs stated that the federal government has "adapted the basic principle that [says] it is a fundamental right of Canadians regardless of their economic circumstances, to enjoy adequate shelter at reasonable cost." The Ontario Ministry of Housing declared that "adequate housing at affordable prices is a basic right of all residents of Ontario". (p. 17)

The emphasis, once housing policy became concerned with affordability in the mid-sixties, began to change with respect to those whom policy was attempting to assist. The 1964 revision of the National Housing Act gave active encouragement to public housing aimed at the lowest income groups. Fallis (1980) characterizes the approach to housing policy taken in the 1960's:

> Households in the upper third of the income distribution received no direct assistance, operating wholly in the private market; households in the middle third received a little aid through the

> market failure programs...; households in the lower third received direct assistance under the programs to redistribute income. (p. 21)

Through the later 1960's and 1970's the emphasis of policy shifted, even though distributional considerations prevailed. The Task Force (1979) identified the objectives of housing policy in the early '70's as:

> - stimulation of residential construction for cyclical stabilization purposes,
> - assistance to middle income groups which were experiencing difficulties in buying a house because of inflation,
> - improvement of the community environment in which housing units were placed
> - subsidization of rental production for households whose incomes were not tested. (p. 107)

Similarly, Patterson (1977) suggests:

> This commitment declined between 1971 and 1973 when the National Housing Act was amended to accommodate a host of new programs. Chief among these turned out to be the Assisted Home Ownership Program which was intended to provide shallow subsidies to those families otherwise unable to purchase housing on the market or to those families with incomes in the upper ranges of those normally entering public housing. (p. 294)

The second and the last objectives identified by the Task Force suggest that while an emphasis remained on use of housing policy, the target for the redistribution had shifted. As Fallis (1980) has incisively observed:

> An even more significant change in the organization chart was the growth of programs intended to provide assistance to the middle third of the income distribution.... Housing was beginning to "cost too much" even for the middle-income household.... Indeed, as bizarre as it may sound, the income problems of the middle class became more important than those of the poor. (p. 22)

However bizarre, such an emphasis is not entirely unexpected. It has not been untypical of other housing programs. Stanbury and Vertinsky (1985), for example, argue forcefully:

> That controls may be advocated in the name of the poor, the immobile elderly and disadvantaged minorities. However, their persistence (and indeed their original enactment is largely attributable to the politics of catering to the interests of the much larger number of non-poor, non-elderly and non-disadvantaged.... Rent control is a tribute to the political effectiveness of the middle class... (p. 3-51)

The last phase of housing policy which began in 1975 can best be described as one of retrenchment. The Task Force reports:

> By 1975, pressures on federal loans funds became too great and a policy shift was made from federal financing to the provision of federal subsidies on privately financed housing.... At this time, the federal government also began to withdraw from joint federal-provincial efforts and provincial priorities were reassessed... Provinces also withdrew from federal-provincial public housing as the staggering costs and massive inequity of the program toward individuals became evident. (1979, p. 22)

A similar judgement has been made by the Social Planning Council of Metropolitan Toronto (1984):

> Direct federal spending on social housing has been greatly reduced by the termination of funds for both Section 43 public housing and land banking, and by substitution of private lending capital for direct government financing. The withdrawal of the provincial government has been even more severe. Subsidies to non-profit and co-operative projects have been terminated since 1978. (p. vi)

It is not coincidental that this reaction against the costs of rental housing policies occurred when it did. The beginning of the last phase coincided with the introduction of rent regulation in many provinces, in concert with anti-inflationary controls, implemented by the federal government at that time. The program of rent regulation served to discourage private sector investment in rental housing and thus, increased the potential burdens of financing public sector programs.

3.2 The Instruments of Housing Policy

The use of instruments of housing policy in the past has evolved in distinct stages over which one instrument has gained priority for a limited period of time only to be replaced by another. Moreover, the changing emphasis tends to correspond with changes in the emphasis on the goals of housing.

From its beginnings in 1919, to well into the post-World War II period, the most emphasized instrument of housing policy consisted of the use of direct lendings. During that period, housing policy was directed toward housing construction for the dual purposes of stimulating the economy and alleviating perceived scarcity of housing. At various times, subsidized loans were made available to the provinces and builders to encourage rental housing and also to owners to encourage home ownership.

A break with this approach occurred with the federal-provincial partnership of 1949 by which the federal government agreed to subsidize 75 percent of the capital and operating costs of public housing supplied by provincial governments. As a consequence, the provinces began to direct their policies toward the provision of public housing. Still, the change in emphasis was not abrupt. The 1954 revision to the National Housing Act introduced measures such as mortgage insurance which was meant to encourage home ownership. Moreover, despite the introduction of federal subsidies under the partnership agreement of 1949, only 6,100 units of public housing were produced in Ontario from 1950 to 1964 (Dennis and Fish, 1972, p. 147).

The most substantial shift in focus of CMHC from market efficiency toward redistribution occurred with the revision of the federal-provincial partnership in 1964, which strengthened public housing under arrangements through which the federal government provided 90 percent of capital grants and shared 50 percent of the operating losses for provincial or municipal public housing. The emphasis on redistribution was extended in 1969 with the addition of another instrument in the form of the rent supplement program directed toward "low income households residing in private rental accommodation" (Government of Canada, 1985, p. 8).

The most recent shift in emphasis in housing policy occurred with a much reduced reliance on budgetary policies, requiring government expenditures, together with a concomitant increased reliance on non-budgetary techniques. A major step was the introduction in Ontario of rent regulation in 1975.(4) At the same time, the nature of the federal government's subsidy program for rental housing changed. The emphasis was shifted away from direct subsidy to guarantee and from capital subsidy to operating subsidy. The 1973 measures replaced the capital grant element of public housing with 100 percent loans to non-profit amd cooperative housing. The program was further modified in 1975 to limit the federal government to making a subsidy equal to the difference between the rent and 25 percent of income. Subsequently, this subsidy was modified to be equal to the difference between mortgage amortization cost at market and at 2 per cent so as to i) reduce the rent to lower end of market and ii) assist low income tenants.

In one sense, this historical review has been overly selective to the extent it suggests that housing policy uses only one or few instruments at a time. At any time, rental housing policy consists of a selection of programs, some emphasized, some active and some inactive. The Appendix to this Chapter, for example, lists and describes the current and earlier rental housing programs of the Ontario and federal governments as of 1984. As can be seen, the variety of programs is substantial.

This short historical review of the instruments of rental housing policy fulfills two purposes. First, it shows that the past record of policy demonstrates a changing use of different instruments of policy. Second, it suggests that some correspondence exists between the objectives currently being pursued and the instruments currently used for the purposes of housing policy.

4.0 Policy Toward Ownership of Housing

Even though a distinction can be drawn between rental housing policy and home ownership policy, a complete separation of these policies cannot be justified. The effects of rental policies spill-over onto owner-occupied housing, as does the effects of ownership policies onto the rental market. Moreover, policies toward ownership use government resources and create effects on the distribution of income. For these reasons, some knowledge of ownership policies and their effects are required background for the analysis of policies toward rental housing.

Rental housing and owned housing are alternative ways of satisfying a household's demand for housing. Indeed, a given housing unit can supply housing services to either an owner or to a renter. More generally, however, as Table 1.2 shows, the choice between rental and ownership follows a life-time pattern by which young households tend to be renters and the proportion of homeowners increases by age. Such a pattern is not immutable but depends, in part, on policies directed at both home ownership and rental markets.

TABLE 1.2

Tenure Choice by Age in Ontario, 1971

Age	Percentage homeowners
0-24	11
25-35	45
36-44	73
45-54	76
55-65	76
66+	72
Average	62

SOURCE: Fallis (1980) p. 114.

Policies in rental markets that affect the level of rents have both an income and a substitution effect which alter the choice of tenure. Consider a policy which lowers the level of rents. Household income becomes higher in real terms because the price of one of the major components of household consumption has decreased. Most evidence suggests that the incidence of homeownership increases directly with the level of household income. If nothing else, the higher real income makes it easier for the household to accumulate the resources necessary to acquire a house of its own. The substitution effect counteracts the income effect. The lower level of rent makes rental housing cheaper relative to homeownership, leading the household to prefer to remain in rental accommodation. The overall effect of lower rent levels on the choice of housing tenure reflects the comparative strength of the income and substitution effects. The point, however, remains that rental housing policies spill-over onto the choice of homeownership.

Similarly, housing policies directed toward ownership have effects that extend to the rental housing market. Any tax or subsidy policy that reduces the costs of home ownership creates an incentive for households to switch from renting their accommodation to owning their own homes. This switch has an initial effect of reducing the level of rents because of the reduced demand for rental housing.

The analysis of the effects of rent regulation on choice of tenure adds a further dimension to the analyses. Some households which occupy controlled rental units benefit from the policy through paying lower than market determined rents. The income and substitution effects described above apply fully to this group of households. Other households which do not occupy controlled units may end up paying higher rents than they would have in the absence of rent regulation because either they could not find housing at rental levels covered by the controls and were required to occupy more expensive housing or, because the presence of controls forced up the rents in uncontrolled markets.(5) For these households, the income and substitution effects work the other way. The higher rent reduces real income and the household's ability to accumulate resources to purchase a home whereas the higher rent makes the relative cost of owner-occupied housing cheaper. As indicated in Section 1.1, the effects work both ways. Just as rental housing policies affect homeownership, so too, homeownership policies are an important influence in the rental housing market.

The above analysis establishes the point that ownership and rental housing policies should not be considered in isolation. Literally, policies directed toward encouraging homeownership could be included among the policies complementary to policies for rental housing. For present purposes, the majority of attention will be focussed on rental market policies as complements to rent review.(6)

One further reason for considering ownership policies in this study remains to be discussed. Throughout this study, judgements will be made about the costs and redistributive effects of various rental housing policies. Yet, these effects of rental housing policies should not be judged in a vacuum. Ownership policies also are costly to governments, either through requiring direct expenditures on subsidies or through foregone taxation revenues through favoured tax treatment. Moreover, the benefits of ownership policies are not uniform among households. Rather, the impact of ownership policies differs according to income group. Thus, the study of the effects of ownership supplies a perspective for judging the costs of rental housing policies and their incidence across income groups.

5.0 Taxation and Housing Policy

Taxation policies permeate every sector of the economy in terms of their effects. Just as some recognition must be given to homeownership policy in any study of rental housing, so too, attention must be directed toward taxation as an influence in the rental housing market. Later, in Chapter 5, the effects of the rental housing market of the Multiple Unit Residential Building Program (MURB) and the treatment of depreciation are treated explicitly in some detail as examples of supply augmenting policies. Other aspects of the impact of taxation on the household's choice between rental housing and homeownership will be considered in the following sections. First, however, it is necessary to outline the changes to the Canadian tax system which occurred in 1971, in order to provide a perspective on subsequent changes in the tax treatment of rental and owner-occupied housing.

5.1 Federal Tax Reform: 1971

The federal government, in response to the report of the Carter Royal Commission on Taxation, revised the taxation system in a number of ways which affected both rental housing and homeownership:

- the introduction of a capital gains tax for gains on the financial and real investment except for the sale of a principal residence, with half the gain treated as earned income;
- the creation of a separate depreciation class for each rental building with depreciation being recaptured and treated as income in the event of a sale of a depreciable asset above depreciated value;
- the elimination of the use of real estate as a tax shelter for non-real estate income by

> prohibiting real estate losses to be used to offset other income, and
>
> - the deemed realization on death of half the difference between depreciation cost and practice value on real estate holdings. (Smith, 1977, pp. 25-26)

Smith judges that:

> The implications of these revisions for housing are quite profound...[and] reduce the desirability of investment in residential rental property and encourage homeownership. (Smith, 1977, p. 26)

The encouraging effects to homeownership are quite clear. An owner-occupied residence becomes, as a result of the changes, one of the few assets on which the owner would not be subject to capital gains taxation on any increase in value.

The effects of these changes on the supply of rental housing requires further explanation. As Smith (1977, p. 27) notes, some of these changes were shared with other types of investment. In particular, the introduction of the capital gains tax affected most forms of equity investment. More significant for real estate alone were the elimination of the use of real estate as a tax shelter and the deemed realization on death of one-half the gains on real estate holdings. These changes reduced the attractiveness of investment in real estate. Smith points out that by December 1974, private multiple dwelling starts had dropped to 56% of their 1969 level. Whatever the intended effects of these changes, they appear to have been detrimental from the standpoint of rental housing.

The 1971 taxation revisions raise an important issue which will arise later in the discussion of supply augmenting policies. From what base should the tax treatment of residential housing be judged? A great difference exists between results from using the pre-1971 and the post-1971 tax system. For example, the sheltering of non-real estate income by real estate losses was a normal feature of the pre-1971 system. From this perspective, the Multiple Unit Residential Building (MURB) program restored a sheltering provision which was temporarily removed. On the other hand, if the post-1971 system was used as a base, the MURB provisions would reflect a special provision directed toward residential housing. The former interpretation gains further credibility in that the removal of the tax shelter affected small investors in real estate to a greater degree than larger. From this perspective, the MURB program then could be interpreted as a device to extend the same privileges to all investors in real estate.

5.2 Taxation and Housing Choice

A residence can be viewed as an investment by a household similar to its investment in stocks, bonds and other income earning assets as well as other assets such as fine art, automobiles and consumer durables. The household holds each of these assets in the anticipation that it will receive a return from that investment. The yields on securities such as stocks and bonds come in the form of explicit income such as dividends and interest or as capital gains which result from changes in value. In contrast, the returns from real assets such as paintings, automobiles and housing come in the form of services in kind: enjoyment of fine arts, transportation and housing. Real assets also can change in value so as to yield capital gains.

The tax system in Ontario and Canada treats the income in kind from durable assets such as housing, fine art, consumer durables and automobiles differently than income gained from financial securities. As Fallis (1980) notes:

> Under current law in Ontario and all of Canada, the value of the flow of services from owned housing, which is income in kind to the taxpayer, is exempt from taxation. Similarly, the service flow or imputed income from owning any real asset, a car, a boat, jewellry or a painting is not taxed. The imputed income from housing, however, is by far the largest part of such income. (p. 105)

Comparable treatment of income in kind from housing with income from other forms would require that the gross value of the imputed rent be fully taxable with deductions permitted from this gross value for expenses incurred in earning that income such as maintenance, depreciation, property taxes and interest expense.(7)

Fallis presents the example shown in Table 1.3 to illustrate the consequences of the treatment of the imputed income for the choice of housing tenure. He considers two households with identical income of $18,000 and accumulated savings of $10,000. One household invests all the savings in a bond and rents, one acquires a $10,000 equity in a house and the third acquires a $5,000 equity in a house and invests the other $5,000 in a bond. In addition each household has a basic exemption of $3,000 for the personal income tax.

Table 1.3 clearly demonstrates the difference in treatment of income in kind from housing and other forms of investment income. The final row presents the amount of disposable income which remains after the payment for housing. Comparison of these figures shows that the amount that each household has available after taxes and housing expenses depends directly on the level of its equity held in housing. The owner with $10,000 equity has $7,000 to spend for purposes other than housing. Whereas, the owner with $5,000 equity has $6,800 and the owner without any equity has only $6,600.

Homeownership offers a further tax advantage to households in that capital gains on principal residences are exempt from taxation income. This treatment can be compared with that of capital gains on most other assets which are taxed at one-half the rate applied to other income. Fallis (1980) describes the effects of this treatment:

> The immediate impact of the exemption, before markets have adjusted, is straightforward. Any household that realized a capital gain enjoyed an increase in wealth equal to one-half the capital gain multiplied by the taxpayer's marginal tax rate. (p. 126)

He goes on to estimate that the average tax increase from the elimination of the tax exemption was $355 in 1971, a year in which housing prices in Ontario rose at 7 per cent. He concludes that:

> The benefit is much smaller than from the exemption for imputed income and smaller than from most homeownership programs... The capital gains exemption is...regarded as the most important aspect of public policy related to housing. These results suggest this is not the case. (1980, p. 127)

The favourable tax treatment of homeownership has a number of implications for the working of the residential housing market. Most are beyond the scope of this study which examines rental housing policies and their effects.

TABLE 1.3

Comparative Positions of Taxpayers by Housing Tenure and Financing

	Renter ($)	Owner with $10,000 equity ($)	Owner with $5,000 equity ($)
Income			
Earnings	18,000	18,000	18,000
From financial assets	1,000	---	500
Imputed from housing assets (net)	---	(1,000)	(500)
Taxable income	16,000	15,000	15,500
Taxes	3,400	3,000	3,200
Disposable income	12,600	12,000	12,300
Housing expenditures			
Rent	6,000	---	---
Mortgage interest	---	4,000	4,500
Ownership expenses	---	1,000	1,000
After-housing disposable income	6,600	7,000	6,800

NOTE: Assume that the house has a market value of $50,000 and there are $1000 annual costs associated with home ownership (there is no depreciation); the house rents for $6000 a year (derived from assuming that the long-run net return to housing is m [the mortgage rate] and that the house has $1000 in annual operating costs); the mortgage rate of interest is 10 per cent; the rate of interest on bonds is 10 per cent; the taxpayer has an average tax rate of 20 per cent up to $15,000 and a marginal tax rate of 40 per cent beyond; and the taxpayer has $3000 in deductions.

SOURCE: Fallis (1980), Table 24, p. 107.

The income distribution effects of this tax treatment require further examination because they provide a perspective from which any effects on income distribution arising from rental policies can be judged.

Fallis (1980) has estimated the effects of the tax treatment of imputed income from housing on the distribution of income.(8) The approach used by Fallis compares the effects of replacement of the favourable tax treatment of housing with a program of equal expense in terms of foregone revenue which offers benefits which are proportional to income. The results of this comparison presented in Table 1.4 show that low income households (up to $8,000) would be harmed and higher income households benefitted by the replacement of the present treatment of income in kind from housing with a proportional alternative. This measure only captures the benefits to a representative household in each income group. The greater incidence of benefits to lower income housing was offset by the fact that homeownership rises with income. Positive benefits from this feature of the tax system are gained by virtually all homeowners. The increase of homeownership with income means that more of the benefits go to higher income groups than indicated by the simple comparison in Table 1.4.(9)

TABLE 1.4

Distribution by Income Class of Benefits from the Exemption of Imputed Income, Homeowners, Ontario 1971

		Average differential benefits ($)	Differential incidence	
Income ($)	Distribution of home-owners (%)	Market value measure	Market value measure	Homeowners as a percentage of the entire class
0-1,999	6	-327	-0.272	49
2,000-3,999	8	-305	-0.101	52
4,000-5,999	7	-201	-0.040	45
6,000-7,999	10	-131	-0.018	54
8,000-9,999	13	25	0.003	57
10,000-11,999	14	42	0.004	63
12,000-14,999	17	123	0.009	72
15,000-24,999	20	141	0.008	79
25,000+	5	293	0.009	92

SOURCE: Fallis (1980), Table 26, p. 115.

6.0 Organization of the Study

The remaining chapters of this study are directed toward two separate themes. Chapters 2 and 3 are devoted to developing a framework for assessing the impact of different types of housing policies on the rental housing market. As mentioned earlier, a system of classification of housing policies is developed in Chapter 2 so as to permit the avoidance of the excessive detail of a policy-by-policy review. Chapter 3 provides a more detailed exposition of the assessment criteria which have been discussed in summary form in sections above.

The remaining chapters are devoted to applying the framework developed in Chapters 2 and 3 to the assessment of rental housing policies. Chapter 4 applies the criteria to various forms of rental housing allowances, the policy chosen to represent demand augmenting policies. Chapter 5 uses the framework to assess supply augmenting policies. Chapter 6 reviews two forms of market replacing policy: public housing and non-profit housing programs. Chapter 7 gives a different perspective on rental housing policies by providing a comparative analysis. The basis of the comparison consists of the simulated effects of $200 million additional expenditure on each of the primary policies: housing allowances, general subsidies and public housing. Attention is concentrated on the effects on adequacy of income and adequacy of housing because these are the ones which are amenable to quantification. Finally, Chapter 8 summarizes the most significant findings of the study.

Notes to Chapter 1

(1) The word "instrument" is used here to denote a single policy such as rent regulation, housing allowances or supply subsidy to distinguish these policies from overall housing policy which represents a blend of individual policies.

(2) This review of housing policy considers only the evolution of policies which are complementary to rent regulation in keeping with the overall emphasis of the study. The history of rent regulation in Ontario has been surveyed in Stanbury and Thain (1984).

(3) The emphasis on federal programs results because many provincial programs have developed as a response to federal initiatives.

(4) See Stanbury and Thain (1984) for a discussion of the events leading to this step and Stanbury and Vertinsky (1985) and Smith and Tomlinson (1981) for analysis of the effects of rent control.

(5) Fallis and Smith (1985) show that the rent level in the uncontrolled sector was between 125 and 130 per cent of the rent in the controlled sector. They estimate that between 50 to 60 per cent of the difference can be explained through the effects of rent control with the remainder accounted for by quality differences.

(6) The failure to consider more fully the impact of ownership policies on the rental housing market represents a limitation of this study. The importance of this limitation depends on the nature of the adjustment process in the rental housing market. As will be shown in later chapters, the level of rents will be determined by supply factors if rental housing can be readily expanded over the long run without any increases in costs. Demand factors are more important in determining rents if additional housing can be increased only with substantial increases of cost relative to existing housing. Appendix 1 to Chapter 7 suggests that the supply of rental housing can be readily expanded in the long run without major increases in cost. If this perception is correct, ownership policies can have a significant impact on the level of market rents only in the short run.

(7) The taxation of imputed rent on housing is even more favorable in the United States. Even though imputed rent is not taxed, households can deduct mortgage interest and property taxes from gross income. See Aaron (1972), pp. 53-55.

(8) The effects of the capital gains exemption on the distribution of income are not presented. Any calculation depends on the relationship between the price paid when the housing was purchased and the price

paid when sold. The results could vary widely according to the years chosen. Moreover, as already stated, the effect is much smaller than the effects of the treatment of imputed income.

(9) This conclusion must be tempered by an awareness that some of these benefits will be passed on to renters because of the interrelation between the rental and ownership markets. As discussed above in footnote 6, this spill-over will be smaller, the more responsive is the supply of rental housing to the level of market rents. The evidence in the appendix to chapter 7 suggests that this responsiveness is quite great. As a consequence, the spill-over of the effects of homeownership policies is likely to be small in the long run.

Appendix to Chapter 1: Description of Rental Housing Programs

by Pearl Ing

This section provides a description of rental housing programs in Ontario. The focus is on federal and Ontario provincial programs. Since this paper studies rental housing programs which affect Ontario, we do not discuss programs which have been initiated by other provinces. Tables 1 and 2 list the programs initiated by the federal and Ontario governments, respectively. A concerted effort has been made to list all past and existing programs, however, because of the large number and variety of programs, some omissions may occur. Descriptions, identifying the key features and other interesting points of the programs, follow. For simplicity's sake, we begin with descriptions of federal rental programs and then, go into descriptions of Ontario (provincial) rental programs. The possibility exists that the analysis of programs and changes which may have occurred in the programs are not all documented. It should be emphasized that this paper does not claim to be the complete authority on Canadian rental housing programs.

Table 1: Federal Rental Programs

Limited Dividend Housing Program

Insured Loans for Rental Housing Program

Mortgage Insurance Program [MIP]

Public Housing Program

Federal-Provincial Rural and Native Program [RNP]

Non-Profit Cooperative Housing Assistance Program

Non-Profit Housing Assistance Program

Residential Rehabilitation Assistance Plan [RRAP]

Multiple Unit Residential Buildings [MURB]

Assisted Rental Program (privately funded) [ARP]

Private Non-Profit Housing Corporations Assistance Program

Graduated Payment Mortgage [GPM]

Canada Rental Supply Plan [CRSP]

Community Resource Organization Program [CROP]

Department of Veteran Affairs Housing Program for Veterans

Federal-Provincial Rural and Native Program [RNP]

Municipal Incentives Grants

All these programs are described in some depth in the following pages.

Table 2: Ontario Rental Programs

- The Elderly Persons Housing Aid Act
- Student Housing
- Rent Supplement Program
- Accelerated Family Rental Housing Program
- Community Integrated Housing Program
- Private Assisted Rental Program
- Ontario Rental Construction Grant [ORCG]
- Municipal Non-Profit Housing Program
- Ontario Rental Construction Loan Program [ORCL]
- REnt HAB/Demonstration Projects
- Innovative Rental Construction Loan Program [Inno Rent]
- Northern Ontario Assistance in Housing [NOAH]
- Wigwamen Incorporated
- Neighbourhood Improvement Program [NIP]
- Convert-to-Rent
- Ontario Renews - Adding Rental Units to Existing Housing
- Municipal Incentive Grants Program
- Community Sponsored Housing Program
- Ontario Community Housing Assistance Program [OCHAP]

All these programs are described in some depth in the following pages.

Description of Federal Programs:

Program:	Limited Dividend Housing Program
Date Started:	1938 (but was only used significantly after 1967)
Date Ended:	No activity since 1981
Enabling Legislation:	Fed.: National Housing Act, Section 15
Administered by:	Canada Mortgage and Housing Corporation (CMHC)
Objective:	To increase the supply of moderately priced rental accommodation

Description:

The program began in 1938 and was altered a number of times during its existence. However, it was only used in a significant way after a mid-1960s revision. The program, as it existed after this revision, is outlined below.

To promote the development of moderately priced rental accommodation, CMHC offered loans to finance the construction and purchase or improvement of existing buildings. The loans were for 95 per cent of a project's capital costs and were at a below market rate of interest. In return for the loans, building owners had to agree to allow CMHC to control rents in the building. The rents set by CMHC allowed building owners an acceptable rate of return on their investments but were still affordable for low income households. Only households within specific income groups were allowed to rent units made available through the program. For a minimum 15-year period, building owners could only raise rents with CMHC's consent. After the 15-year period, the building's owner could opt out of the agreement, but only if the loan had been repaid. This program was replaced by the Assisted Rental Program (ARP) in 1976.

Program: Insured Loans for Rental Housing Program

Date Started: 1946

Date Ended: Still Operational

Enabling Legislation: Fed.: National Housing Act (NHA), Part 1, section 6

Administered by: Canada Mortgage and Housing Corporation

Objective: To encourage the development of new rental housing by assisting in its finances

Description: Long term loans authorized by the NHA are available to finance the development of new rental housing. These loans can be for up to 95 per cent of the value of a project. Two types of insured loans are available for rental housing: the NHA-Approved Lender Loans (once referred to as the Loan Insurance Program) and CMHC Loans (once referred to as the Residual Lending Program). Approved lender loans are loans provided by private companies under the terms of the NHA. CMHC loans are loans directly from CMHC which are provided when financing from approved lenders is unavailable. Generally, the loan covers a period of five years, but can be longer and may coincide with the amortization period which is usually 25 to 35 years. The interest rate for loans is negotiable.

Program: Mortgage Insurance Program [MIP]

Date Started: 1954

Date Ended: Still Operational

Enabling Legislation: Fed.: National Housing Act, 1954

Administered by: Canada Mortgage and Housing Corporation

Objective: To facilitate the availability of mortgage funds for new construction by protecting lenders from costs incurred due to borrower default

Description: This program constitutes CMHC's principal business activity. It applies to both the ownership and rental sectors. Only details relating to the rental component of the program are covered here. Borrowers can usually obtain a lower interest rate, longer amortization period, and a higher loan-to-value ratio for low or moderate priced housing than is available in the standard non-CMHC-insured lending field. The program is financed by insurance fees paid by the borrower. By law, all mortgages over 75 per cent of the value of the property, made by institutional lenders, must be insured.

NHA insured loans may be as high as 95 per cent of the first $50,000 of lending value for a new or existing home plus 75 per cent of the balance to a maximum of $70,000 (in 1980). Builders of rental units with 10 per cent equity pay 1.25 per cent for an installment loan or 1.125 per cent for advanced lump sum loan. Rental loans require 10 per cent equity.

In 1982, the 1.25 per cent base premium for rental loans was based on a loan level at 85 per cent of market value. An incremental premium schedule applies to loans in excess of the 85 per cent level. A surcharge is payable when loan advances are made before completion of construction and occupancy, and where the borrower elects to repay on a graduated payment basis. The maximum insured loan cannot exceed 80 per cent of cost on new construction, and 75 per cent of cost on GPM loans.

This program replaced an earlier joint lending technique.

Program: Public Housing Program

Date Started: 1964

Date Ended: New commitments for Ontario ceased in 1978

Enabling Legislation: Fed.: National Housing Act, Sections 44(1) and 6.
Prov.: Housing Development Act, Section 6, Ontario Housing Corporation Act, Sections 6(2), 7, 8(1) and 10(1)(b).

Mun.: Resolution of Council, agreement with Province under the Housing Development Act.

Administered by: Canada Mortgage and Housing Corporation/-Ministry of Municipal Affairs and Housing

Objective: To provide financial assistance for the development of public housing projects to be occupied by low income families and individuals

Description: Two forms of assistance were available for the development of public housing, before the form of assistance was modified in the late 1970s. These were Long Term Loans and Federal-Provincial Partnership Arrangements. Tenants in public housing developed with both types of assistance paid on a rent-geared-to-income basis and were chosen using a 'point system'.

Long Term Loans: Municipalities had to initiate public housing projects developed under this portion of the program. If a municipality's request for public housing were accepted, the Ontario Housing Corporation would undertake its development. The capital cost of building public housing was provided through loans from the federal and provincial governments, 90 per cent and 10 per cent, respectively. Operating subsidies were provided by the federal, provincial and municipal governments, 50, 42.5 and 7.5 per cent, respectively. Project management was undertaken by either the Ontario Housing Corporation or the local housing authority.

Federal-Provincial Partnership Arrangements: The development of public housing under this portion of the program was a joint undertaking of the two senior levels of government. Municipalities also participated in some cases. Responsibility for public housing development was divided among the governments according to mutual agreement. The capital cost of building public housing was provided by the federal and provincial governments which provided 75 and 25 per cent, respectively. Municipalities could be requested to share the provincial cost. Any operating deficit was shared by the participating governments on the same basis as the capital costs.

In the late 1970s, assistance provided for public housing was modified. Two types of public housing were developed; Municipally-sponsored and Provincially-sponsored. In both cases, up to 100 per cent of tenants pay on a rent-geared-to-income basis and include both families and senior citizens.

Municipally-Sponsored:
Under this portion of the program a municipal housing corporation may obtain mortgage financing up to 100 per cent of the cost of building or acquiring moderately priced rental housing. The loans are arranged from a NHA-approved private lending institution. These developments are managed by the municipal housing corporation.

Provincially-Sponsored:
Under this portion of the program the Ontario Housing Corporation may obtain up to 100 per cent of the cost of building or acquiring moderately priced rental housing. The loans are arranged from a NHA-approved private lending institution. These developments are managed by the municipal housing corporation. The province only provided rental housing under this program when the need for it has been shown and municipal or private non-profit corporations and cooperatives have not met the need.

Program: Federal-Provincial Rural and Native Housing Program [RNP]

Date Started: 1974

Date Ended: Still operational

Enabling Legislation: Fed.: National Housing Act, Sections 34.1, 40, 36(g) and 37.1.
Prov.: Housing Development Act, R.S.O. 1970 Section 6(1); Ontario Housing Corporation Act R.S.O. 1970 Section 6(2)

Administered by: Canada Mortgage and Housing Corporation

Objective: To provide new housing and renovation assistance to low-income native and non-native families.

Description: The ownership/rental component of the program provides a loan to finance the construction of a house and subsidizes the difference between loan amortization costs and property taxes, and 25 per cent of the household income. The federal and provincial governments share the loan and subsidy costs, 75 per cent and 25 per cent respectively.

A renovation component provides a loan to finance the upgrading of a house to meet minimum health and safety standards and to preserve its livability for at least 15 years. The emergency repair component provides a one-time grant to make necessary health and safety repairs. The rehabilitation and emergency repair programs are financed by the federal government alone.

Program:	Non-Profit Cooperative Housing Assistance Program (or Section 56.1 Non-Profit and Cooperative Housing Program)
Date Started:	1978
Date Ended:	Still Operational
Enabling Legislation:	Fed.: National Housing Act, Section 56.1 as amended
Administered by:	Canada Mortgage and Housing Corporation
Objective:	To encourage and assist in the development of cooperative housing by providing loans
Description:	Two types of housing cooperatives are provided for under the terms of the National Housing Act: building cooperatives and continuing non-profit cooperatives. The former is usually composed of a group of people who pool their resources in order to obtain individual moderately priced home-ownership. On the other hand, a continuing non-profit cooperative is composed of a group of people who collectively own and manage some form of housing in which units are leased. There are three types of assistance available to cooperatives under the program: start-up funds, loans and annual assistance.
Start-up Fund:	Start-up funds of up to $75,000 are available to cooperatives to help them prepare an application for fundings.
Loans:	Cooperatives are encouraged to arrange a NHA insured loan for up to 90 per cent of the cost of a project from an approved lending institution. CMHC may provide a second mortgage loan to make up the difference between a 90 per cent NHA insured loan and a project's cost. CMHC may also act as a lender of last resort, if a cooperative cannot borrow from an approved lender.
Annual Assistance:	CMHC will provide annual assistance to offset the operating losses of a non-profit cooperative. At its maximum, the assistance will be equal to a interest reduction of one per cent on a 90 per cent mortgage with a 35-year term, or down to two per cent on a 100 per cent mortgage for the same term.

Cooperatives are encouraged to purchase existing structures rather than building new ones. The cooperatives must adhere to maximum price and unit size limits. Rents for units are set so that tenants do not pay more than the market rent for similar accommodation.

Section 56.1 programs replaced the programs funded under Section 15.1 and 34.18 (see Non-Profit Housing Assistance Program).

Program: Non-Profit Housing Assistance Program (or Section 15.1 Non-Profit and the Section 34.18 Cooperative Programs)

Date Started: 1973

Date Ended: 1978

Enabling Legislation: Fed.: National Housing Act, Sections 15.1 and 34.18

Administered by: Canada Mortgage and Housing Corporation

Objective: To provide financial assistance to allow non-profit organizations to develop low cost rental housing and to increase the supply of housing available to low-income families, senior citizens and special groups (i.e., the handicapped)

Description: Under this program charitable and municipally owned non-profit organizations received assistance to develop housing. There were three types of assistance available; start-up funds, loans and CMHC contributions.

Start-up Funds: Start-up funds of up to $10,000 were available to non-profit organizations, which were not provincially or municipally owned, to ensure the group would be able to prepare an application for funding in the proper manner.

Loans: Loans were available to cover 100 per cent of the lending value of a project if it was owned by a charitable or municipally owned non-profit organization and 95 per cent of the lending value of a project, if it was owned by a provincial organization. The repayment term of the loans could be up to 50 years.

CMHC Contributions: Non-profit organizations making use of the loan portion of the program could apply for a contribution from CMHC which would not exceed 10 per cent of the cost of the project or alternatively they could enter into a land lease agreement ("ground rent subsidy") with CMHC which would own land for the project. The 10 per cent contribution by CMHC had to be applied to reduce the loan.
CMHC had to approve any rent increase in housing projects receiving assistance under the program.

Program: Residential Rehabilitation Assistance Plan [RRAP]

Date Started: 1973

Date Ended: Still Operational

Enabling Legislation: Fed.: National Housing Act, Part IV.1

Administered by: Canada Mortgage and Housing Corporation and local municipalities

Objective: To provide funds to revitalize deteriorating housing units through loans and grants to homeowners, landlords, non-profit and cooperative organizations in designated urban and rural areas.

Description: Homeowners with adjusted family incomes of up to $6,000 are eligible for the maximum loan ($10,000) and loan forgiveness ($3,750). As incomes increase between $6,000 and $11,000, the amount of loan forgiveness decreases. Homeowners with larger incomes repay loans in full. Loan forgiveness is earned at the rate of $750 for each year the homeowner continues to occupy the dwelling.

Landlords who arrange private rehabilitation loans may be eligible for a fully forgiveable CMHC loan of up to $2,500 per family housing unit in return for CMHC determined rent limitations.

Non-profit and cooperative organizations that arrange private rehabilitation loans may also be eligible for a fully forgiveable CMHC loan of up to $3,750 per family housing unit. Rehabilitated non-profit, cooperative and private rental units can only be sold with CMHC consent.

Program: Multiple Unit Residential Buildings [MURB]

Date Started: 1974

Date Ended: Extended several times, terminated in 1979. Reintroduced in 1980, terminated in December 1982.

Enabling Legislation: Fed.: Income Tax Regulations

Administered by: Canada Mortgage and Housing Corporation

Objective: To encourage the development of multiple unit residential buildings for rental purposes

Description: The MURB program was a tax deferral program in which owners of eligible rental units could defer non-rental income tax owed by writing off certain 'soft costs'* (that would have been incurred during construction) and by using a Capital Cost Allowance (CCA) on an ongoing basis. A MURB owner could deduct a loss created by a unit's depreciation (to the maximum CCA) from other income.

Three types of MURB ownership were available to investors. They were:

i) Undivided Ownership - an investor could buy a share of an association or partnership which held a MURB as an asset,

ii) Divided Interest - an investor could purchase an eligible unit and hold the title to the unit itself,

iii) Limited Partnership - an investor could become a limited partner in the ownership of a MURB with a general partner who would operate the property.

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*'Soft costs', as defined by the government, included:
- promotion expenses
- mortgage fees
- legal and accounting fees
- interest expense during construction
- interest and property taxes.

Program: Assisted Rental Program (privately funded) [ARP]

Date Started: 1975, modified 1978

Date Ended: 1978

Enabling Legislation: Fed.: National Housing Act, Section 14.1, Part 1

Administered by: Canada Mortgage and Housing Corporation

Objective: To stimulate the construction of moderately priced rental housing by attracting more private capital

Description: Loans of up to $1200 annually per unit were provided to reduce rent levels (required by development costs) to the existing market rents of similar existing units. The amount of the loan depended on the number of units in a project, construction costs, mortgage interest rates, operating costs, and the average rents for similar units in the proposed construction area. The loans were for up to 15 years and were interest-free for 10 years or the support period, whichever was longer. The loan had to be repaid if a project was sold or refinanced or one year after the assistance ended. By the end of the first mortgage's amortization period, the loan had to be repaid.

The Assisted Rental Program was modified in 1978. As with the earlier version of the program, assistance was provided to reduce rent levels on new rental units to the market rental rate charged for similar existing units. Assistance was provided through the modified program in the form of "Payment Reduction Loans". These loans were second mortgage loans which could not exceed an amount equal to $2.25 per month for each $1000 of the first mortgage in the first year. The rate of interest on the payment reduction loan was the same as on the first mortgage. The first mortgage had to be NHA-insured, represent 90 per cent of a project's costs, have a term of at least five years and have an amortization period of 25 to 35 years.

The amount of the second mortgage advances was gradually withdrawn at a rate producing a constant 5 per cent increase in the borrower's net principal and interest payments annually.

The 1978 version of the Assisted Rental program was to provide assistance similar to the Graduated Payment Mortgage plan which was introduced later in 1978. This version of the Assisted Rental Program was a transitional program; it was to be phased out as the Graduated Payment Mortgage plan developed.

Program: Private Non-Profit Housing Corporations Assistance Program (or Section 56.1 Non-Profit and Cooperative Program)

Date Started: 1978

Date Ended: Still Operational

Enabling Legislation: Fed.: National Housing Act, Section 56.1 as amended

Administered by: Canada Mortgage and Housing Corporation

Objective: To provide assistance to privately owned non-profit housing corporations to help them develop low cost rental housing and to increase the supply of housing available to low income families, senior citizens and special groups (i.e. the handicapped).

Description: This program is a modification of a portion of the Non-Profit Housing Assistance Program (1973). Private non-profit corporations can receive three types of assistance: start-up funds; loans; and annual assistance.

Start-up Funds: Start-up funds of up to $75,000 are available to private non-profit housing corporations to help them prepare an application for funding.

Loans: Private non-profit corporations are eligible for NHA-insured loans from approved lenders covering up to 100 per cent of project costs for terms of up to 35 years. When there is a clear social and cost advantage, sponsors are encouraged to purchase existing structures rather than construct new ones.

Annual Assistance: CMHC will provide annual assistance to private non-profit corporations to offset their operating losses. The maximum amount of the assistance is equivalent to a reduction in the interest rate down to two per cent on a 100 per cent mortgage with a 35-year term.

Private non-profit housing corporations applying for federal assistance must adhere to maximum price and unit size limits. Rents charged must be in line with those charged for similar accommodation in the area, though federal assistance is available for low income families who cannot afford to pay this.

Program: Graduated Payment Mortgage [GPM]

Date Started: 1978

Date Ended: Still Operational

Enabling Legislation: National Housing Act, Section 8(4.2)

Administered by: CMHC

Objective: To reduce mortgage payments during the first years of a mortgage.

Description: A Graduated Payment Mortgage is a NHA-insured mortgage formula with terms which provide for relatively low monthly mortgage payments initially which increase gradually and level out. Under the GPM, initial borrower payments are reduced by $2.25 per $1000 of principal. Annual payments then increase 5 per cent a year, until the end of the tenth year. After the tenth year payments remain the same for the rest of the amortization period. GPM mortgages made by private lenders are insured against default. Direct GPM loans are made on a residual basis. New and existing ownership and rental accommodation subject to CMHC regional price ceilings are eligible.

The Graduated Payment Mortgage replaced the Assisted Rental Program.

Program:	Canada Rental Supply Plan [CRSP]
Date Started:	November 1981
Date Ended:	December 1984
Enabling Legislation:	National Housing Act, Section 14.1
Administered by:	Canada Mortgage and Housing Corporation
Objective:	To stimulate the construction of rental accommodation in areas with low vacancy rates
Description:	Interest-free loans of up to $7500 per unit are available for the construction of rental units in areas of low vacancy rates. In exceptional circumstances, the $7500 per unit limit on loans can be exceeded. The loans are to be secured by a second mortgage and the first mortgage for a project must be insured. There are no size or cost restrictions on the units which can be built with assistance from the programs. Builders receiving assistance from this program must be prepared to enter into an agreement which would make one-third of the units available to low income households under the rent supplement program.

Program:	Community Resource Organization Program [CROP]
Date Started:	June 1973
Date Ended:	Still operational
Enabling Legislation:	Fed.: National Housing Act, Part V
Administered by:	Canada Mortgage and Housing Corporation
Objective:	To stimulate activity in the community-based programs under the NHA by providing financial assistance to resource groups which offer professional and managerial assistance to non-profit and cooperative housing groups
Description:	Grants are available to resource groups which provide professional or technical services to community groups and low-income individuals involved in non-profit and cooperative housing. Groups must meet certain specified criteria, the primary ones being a demonstrated need for housing in the area concerned and a marketing strategy that ensures government funding will be replaced by professional fee income. CROP grants are approved for a period of one year. At the end of this period, the grant is reviewed and may be extended.

Program: Department of Veteran Affairs Housing Program for Veterans

Date Started: 1975

Date Ended: Still operational

Enabling Legislation: Veterans' Land Act; National Housing Act, Sections 34.15, 34.16, Part 1, 15.1

Administered by: Canada Mortgage and Housing Corporation

Objective: To provide better housing opportunities for veterans with moderate incomes

Description: The Department of Veterans Affairs offers additional assistance to veterans qualifying for CMHC housing assistance. Veterans are eligible for a grant of up to $600 annually for five years for the purchase or construction of a new dwelling, if, after direct AHOP or private additional assistance is taken into account, the portion of the veteran's gross family income required for payments of principal, interest and taxes is still greater than 25 per cent of that income. A grant of up to $600 a year for up to five years is offered to veterans who do not qualify for the AHOP interest reduction loan because they want to buy an existing house or for AHOP grants because they do not have a dependent child. (The veteran must obtain an NHA-approved lender loan and must not have owned a house in the previous three years). An additional grant of 10 per cent of capital cost is available for non-profit groups who obtain Section 15.1 loans to develop low rental housing projects intended primarily but not exclusively for veterans.

Program: Municipal Incentives Grants

Date Started: 1975

Date Ended: December 31, 1978

Enabling Legislation: National Housing Act, Section 56.2

Administered by: Canada Mortgage and Housing Corporation

Objective: To encourage municipalities to develop more land for modest-sized housing units at medium density and generally to encourage the economic use of land.

Description: Municipalities can receive a federal grant of $1000 for each unit of eligible housing constructed. The grant is made only for new dwelling units which have received a building permit or its equivalent between November 1, 1975 and December 31, 1978. Dwelling units must meet certain density and size criteria and their value must not exceed the price limit established under AHOP for the municipality issuing the building permit. To be eligible for the grant, dwelling units, whether for rent or for sale, must be constructed for permanent residency, be self-contained and connected to municipal piped services, with roads to a minimum of gravel surface.

Payments in this program were completed on March 31, 1982.

Description of Ontario Rental Programs:

Program:	The Elderly Persons Housing Aid Act
Date Started:	1960
Date Ended:	1976
Enabling Legislation:	Nil
Administered by:	Ontario Housing Corporation
Objective:	To aid in the development of low cost rental housing for senior citizens
Description:	Capital grants were provided to aid in development of low cost rental housing for senior citizens. Charitable organizations and limited dividend housing corporations incorporated by, or on behalf of, a municipality were eligible for assistance. A NHA loan for senior citizens housing had to be obtained before assistance was given. The grants were of either $500 per unit or 50 per cent of the cost, whichever was less.

Program: Student Housing

Date Started: 1966

Date Ended: 1975

Enabling Legislation: Fed.: National Housing Act, Section 46.

Administered by: Ontario Student Housing Corporation

Objective: To provide low cost rental housing for students

Description: Under this program, funds were loaned to various education-related groups to be used to create rental housing for students through construction acquisition or conversion. Groups eligible for assistance under the program included provinces and provincial agencies, municipalities and municipal agencies, universities, colleges, school boards, cooperatives, non-profit corporations and charitable corporations. CMHC provided loans to cover up to 90 per cent of the value of a student housing project and the province provided the remaining 10 per cent.

Program: Rent Supplement Program

Date Started: 1971

Date Ended: Still Operational

Enabling Legislation: Fed.: National Housing Act, Section 44(1)(b)
Prov.: Housing Development Act, Section 2(1)(f); Ontario Housing Corporation Act, Section 6(1).

Administered by: Ministry of Municipal Affairs and Housing and Ontario Housing Corporation

Objective: To provide assisted rental housing for low income families and senior citizens which is integrated into the general community

Description: On behalf of the Ontario Housing Corporation, the province acquires the use of rental accommodation from private landlords. These units are then made available to low income families and senior citizens on a rent-geared-to-income basis. Tenants pay their portion of the agreed-upon rent directly to the landlord. The difference between the reduced rent and the market rent is paid to the landlord by the Ontario Housing Corporation. Generally, the agreement between the Ontario Housing Corporation and the private landlord runs for three years. Up to 35 per cent (+5 per cent for the handicapped) of units in a structure can be included in the program, the other units are rented at market rents. The tenants are chosen by the Ontario Housing Corporation and the landlord from the assisted housing waiting list.

Operating subsidies for the program are provided by the federal and provincial governments, 50 per cent respectively. At one time, municipal governments also contributed to the subsidy and it was divided among the federal, provincial and municipal governments, 50, 42.5 and 7.5 per cent, respectively.

Program: Accelerated Family Rental Housing Program

Date Started: 1974

Date Ended: 1976

Enabling Legislation: Fed.: National Housing Act, Sections 15 and 44
Prov.: Housing Development Amendment Act 1974, Section 2(1)(f), Ontario Housing Corporation Act R.S.O. 1970, Section 6(1)

Administered by: Ontario Mortgage Corporation

Objective: To provide housing for low income households using a rent supplement system and moderate income households using a regulated rent system, which was integrated into the community and privately owned

Description: Builders were provided with favourable first mortgage financing by the Ontario Housing Corporation. In return for their financing builders were required to make 25 per cent of units in a project available to tenants receiving rent supplements. Tenants in these units paid on a rent-geared-to-income basis.

Builders were also required to make the remaining 75 per cent of units in a project available to tenants with specific moderate incomes. The rents charged and rate of return to the builder from the project was subject to controls.

The federal and provincial governments contribute 50 per cent each to the program's operating subsidy. The operating subsidy is needed to cover the difference between the reduced rent paid by tenants on a rent-geared-to-income basis and the market rent.

Program: Community Integrated Housing Program

Date Started: 1973

Date Ended: 1976

Enabling Legislation: Fed.: National Housing Act, Section 44
Prov.: Housing Development Act Section 2(1)(f); Ontario Housing Corporation Act, Section 6(1)
Mun.: Resolution of Municipal Council

Administered by: Ministry of Housing through the Ontario Housing Corporation and Ontario Mortgage Corporation

Objective: To provide assisted rental housing which was integrated into the community and privately owned

Description: The Ontario Housing Corporation provided second mortgage financing to builders to bring the total of the first and second mortgages to 95 per cent of the appraised value of a project. In return for the second mortgage financing, builders were required to make 25 per cent of units in a project available to tenants receiving rent supplements for a period of 15 years. The other 75 per cent of units were rented at market rents. Tenants receiving rent supplements paid rent on a rent-geared-to-income basis and were selected by the Ontario Housing Corporation and the project owner from the assisted housing waiting list.

The operating subsidies for the program, which are needed to cover the difference between the reduced rent paid by tenants and the market rent, are divided by the federal and provincial governments on a 50:50 per cent basis.

Program Private Assisted Rental Program

Date Started: 1976

Date Ended: Still Operational

Enabling Legislation: Fed.: National Housing Act, Section 44
Prov.: Housing Development Act, Section 2(1)(f), Ontario Housing Corporation Act, Section 6(1)

Administered by: Ministry of Municipal Affairs and Housing through Ontario Housing Corporation

Objective: To stimulate private sector participation in the provision of rent-geared-to-income housing units

Description: Through an agreement with the Ontario Housing Corporation, builders finance, construct, own, and manage rental projects which have up to 100 per cent of their units made available to persons on the waiting list for assisted rental housing. The agreements usually are in effect for between 15 to 35 years. Tenants pay rent on a rent-geared-to-income basis and can include both families and senior citizens.

The difference between the rents paid by the tenants and the market rents for the units is covered in a manner similar to that of the Rent Supplement Program. Operating costs of the program are divided equally between the federal and provincial governments. At one time, operating costs of the program were divided between the federal, provincial and municipal governments, 50, 42.5 and 7.5 per cent, respectively.

Program: Ontario Rental Construction Grant [ORCG]

Date Started: 1977

Date Ended: 1981

Enabling Legislation: Fed.: National Housing Act, Section 58
Prov.: Housing Development Act, Section 2(1)(e)

Administered by: Canada Mortgage and Housing Corporation

Objective: To provide additional assistance when the assistance provided under the Assisted Rental Program was insufficient to facilitate the production of moderately priced rental accommodation

Description: The ORCG was intended to complement the Assisted Rental Program. The grants were available to builders if, after they had received maximum assistance from the federal Assisted Rental Program, they could still not produce housing with economic rents. The grant was for up to $600 per unit in the first year and was reduced in each following year based on the same formula as the Assisted Rental Program. The grant was provided over the same disbursement period as the federal program.

The initial rents a builder could charge were set out in the grant agreement. Subsequently, rents would be set by market conditions, but the amount of the grant would decrease as revenue increased.

Program: Municipal Non-Profit Housing Program (or Section 56.1 Non-Profit and Cooperative Housing Program)

Date Started: 1978

Date Ended: Still Operational

Enabling Legislation: Fed.: National Housing Act, Section 56.1 as amended, Section 44(1)(b) and Section 6
Prov.: Housing Development Act, as amended, Section 2(1)(e) and (f)
Mun.: Resolution of Municipal Council, agreement with Province under the Housing Development Act, Section 17(1)(a) and Section 12

Administered by: Ontario Ministry of Municipal Affairs and Housing and Ontario Housing Corporation

Objective: To provide assistance to municipally owned non-profit housing corporations where the main objective is to supply rental accommodation for families and individuals

Description: This program is a modification of a portion of the Non-Profit Housing Assistance Program (1973). Municipally owned non-profit corporations can receive two types of assistance through the program, capital assistance and operation assistance.

Capital assistance is available in the form of NHA insurance on mortgages from NHA-approved lending institutions (which are for up to 100 per cent of the lending value of a project).

Operating assistance is available in the form of an annual federal rent reduction grant to help offset operating losses. At its maximum, the assistance will amount to the equivalent of an interest reduction down to two per cent on a 100 per cent loan over a 35-year amortization period.

Provincial assistance is available to complement the federal assistance. The province will provide, when it is needed, a rent reduction grant of up to 100 per cent of the Federal rent reduction grant. If an additional subsidy is required over and above the federal and provincial rent reduction grants it will be shared equally by the two levels of government.

In structures intended for families up to 35 per cent (+5 per cent for the handicapped) of units may be allocated to tenants who will pay on a rent-geared-to-income basis. In structures intended for senior citizens, up to 50 per cent of units may be allocated to tenants who will pay on a rent-geared-to-income basis. The remaining tenants pay a low end of market rent.

Program: Ontario Rental Construction Loan Program [ORCL]

Date Started: 1981

Date Ended: 1981

Enabling Legislation: Nil

Administered by: Ontario Mortgage Corporation

Objectives: To stimulate the construction of rental housing units in Ontario, especially in areas of the province with low rental vacancy rates

Description: Interest-free loans were available to private builders to finance new rental construction projects and the conversion of non-residential properties to rental accommodation. The loans were second mortgage loans ranging from $4,200 to $6,000 per eligible unit. This amount varied according to the project's final first mortgage rate of interest. The loans had a 25 year term with repayment beginning in the sixteenth year.

To be eligible for a loan under the program, a project had to meet a number of conditions. The conditions included specifications that:

i) new construction projects had to contain a minimum of six units;

ii) up to 20 per cent of units in a complex, but no more than 25 per cent of units in a building, be offered to the local housing authority to be used for assisted housing;

iii) eligible units could be located in mixed residential/commercial or retail projects;

iv) units appropriate for disabled persons be made available if local need warrants it; and

v) a project's units had to fall within set maximum prices.

Program: REnt HAB/Demonstration Projects

Date Started: May 1982

Date Ended: Cancelled in December 1982

Enabling Legislation: Ontario Ministry of Municipal Affairs and Housing

Objective: To encourage the rehabilitation and maintenance of rental housing and the development of new rental units in existing buildings

Description: This program had two components, REnt HAB and demonstration projects.

REnt HAB: This portion of the program was designed to encourage the rehabilitation and maintenance of rental housing. Interest-free loans of up to $7500 were to be available to landlords to "keep and improve" rental units. The loans were to have a 20-year term with repayment beginning in the eleventh year. If a unit ceased to be used for rental housing the loan would have to be repaid at that time.

The REnt HAB loans were to be available only in municipalities with a rental vacancy rate of two per cent or less which have maintenance and occupancy by-laws. To qualify for REnt HAB, units were required to be:
- self-contained
- below minimum standards set in municipal by-laws
- covered by rent review legislation
- occupied prior to January 1, 1976
- rented for less than $750 per month.

Demonstration Projects: This portion of the program was designed to encourage the development of new rental units in existing residential buildings. Interest-free loans of up to $7500 would be available for this purpose. The loans would have a 20-year term with repayment beginning in the eleventh year. The units would have to remain as rental housing for 20 years.

The demonstration was intended to illustrate how constraints encountered, in an attempt to develop new rental units in existing buildings, can be overcome. Constraints included zoning, building and renovation codes and public attitude. Projects were to be of a general nature so that they could be copied or adopted for use in other municipalities. The municipalities slated to be involved in this joint project with the Ministry of Municipal Affairs and Housing were Hamilton, Kingston, Ottawa, Thunder Bay and Toronto.

The program was not actively promoted and lapsed in December 1982.

Program: Innovative Rental Construction Loan Program [Inno Rent]

Date Started: May 1982

Date Ended: Cancelled in December 1982

Enabling Legislation: Nil

Administered by: Ontario Ministry of Municipal Affairs and Housing

Objective: To encourage the construction of moderately priced rental units in areas with rental vacancy rates of two per cent or less, some of which would be available to low income families, senior citizens and physically-disabled persons

Description: Developers and financiers were encouraged to use innovative financial arrangements, mixed land use, and alternative forms of land tenures to develop rental units. Loans were to be made available for new rental projects and for the conversion of non-residential properties to rental units. Each application for a loan was to be evaluated on its "own merit" with special consideration given to the level of assistance required for a project and the degree of innovation exhibited as a project. The loans were to be for a 25 year term and interest-free, with repayment beginning in the sixteenth year. If a project did not remain rental for 15 years the loans were to become repayable with interest.

Projects in municipalities without lot levies or in municipalities which were prepared to reduce lot levies were to be given priority. To be eligible for loans under the program, projects were to be in areas where vacancy rates for rental units are two per cent or less. Projects eligible for the MURB or ORCL program were to be disqualified for loans through the program.

The program was not actively promoted and lapsed in December 1982.

Program: Northern Ontario Assistance in Housing [NOAH]

Date Started: March 1973

Date Ended: December 1973

Enabling Legislation: Fed.: National Housing Act, Sections 43 and 44
Prov.: Housing Development Act, R.S.O. 1970, Section 6, Ontario Housing Corporation Act, R.S.O. 1970, Sections 6 and 7

Administered by: Ministry of Housing, through Ontario Housing Corporation

Objective: To provide low income families in non-urban areas of Northern Ontario, particularly in unorganized and remote communities, with assisted rental housing

Description: Through the Ontario Housing Corporation, which constructs and manages public housing units in Northern Ontario communities, housing is allocated on the basis of need as determined by an OHC point rating system for northern residents. Rental rates are geared to the income of the tenants. CMHC provides a loan to the province of Ontario, equal to 90 per cent of the capital cost of a project and also contributes 50 per cent toward the annual operating subsidy. To cover the remaining capital costs, OHC borrows an additional 10 per cent from the province. OHC subsidizes 50 per cent of the operating deficits.

Program:	Wigwamen Incorporated
Date Started:	March 1973
Date Ended:	December 1973
Enabling Legislation:	Fed.: National Housing Act, Sections 15 and 44 Prov.: Housing Development Amendment Act 1974, Section 2(1)(f); Ontario Housing Corporation Act, R.S.O. 1970, Section 6
Administered by:	Wigwamen Incorporated, with assistance from the Ministry of Housing, through Ontario Housing Corporation and Canada Mortgage and Housing Corporation
Objective:	To assist Canadian native people in meeting their rental housing requirements in Metro Toronto
Description:	Wigwamen Incorporated, a private non-profit organization, purchases housing units for use as rental accommodation with federal funds and is responsible for tenant selection and housing administration. In addition, OHC participates with Wigwamen in a joint committee to select tenants for units that are made available under the Rent Supplement Program. (See also: Rent Supplement Program).

Program: Neighbourhood Improvement Program [NIP]

Date Started: 1973

Date Ended: 1980

Enabling Legislation: Fed.: National Housing Act, Sections 27.1 and 27.3

Administered by: The Ontario Ministry of Municipal Affairs and Housing through its community renewal branch, Canada Mortgage and Housing Corporation and the local municipal authority

Objective: To improve the housing and living conditions of residents of deteriorating neighbourhoods. The emphasis is on rehabilitating individual homes through the federally-sponsored Residential Rehabilitation Assistance Program (RRAP) and facilitating improvement of social amenities, municipal services and public utilities through NIP

Description: The program provides grants and loans to municipalities to encourage the upgrading of older residential neighbourhoods. The NIP program aims at integrating neighbourhood rehabilitation programs with the Residential Rehabilitation Assistance Program's funding of private home reconditioning projects. Neighbourhoods eligible for assistance are those whose housing stock and social and recreational facilities are in need of repair and improvement to comply with minimum standards. Assistance is available to select neighbourhoods and create redevelopment plans, to acquire land for and to construct social and recreational facilities to acquire and clear land for low- and moderate-income housing, and to relocate persons displaced due to neighbourhood improvements. Federal, provincial and municipal governments subsidize the cost of these projects, 50, 25 and 25 per cent (municipalities may borrow from CMHC 75 per cent of their share) respectively.

Additional shared-cost grants are available to municipalities to improve both public utilities and existing commercial establishments in rehabilitated neighbourhoods. This program was changed to the Ontario Neighbourhood Improvement Program [ONIP] in 1982. The ONIP program is modelled on the NIP program with more stringent eligibility criteria.

Program: Convert-to-Rent

Date Started: 1982

Date Ended: Still Operational

Enabling Legislation: Nil

Administered by: Ontario Ministry of Municipal Affairs and Housing

Objective: To encourage the production of 2,600 additional rental housing units by non-residential conversions.

Description: Interest-free loans of $7,000 per unit are advanced in two parts: half at 15 per cent completion, and half on 50 per cent completion. The loan, interest-free for a term of 15 years, is repayable, beginning in year 11, with equal monthly payments over the next five years. All projects must remain as rental accommodation for a minimum of 15 years; otherwise, the loan is immediately repayable in full.

To ensure moderate-rent accommodation, maximum all-included costs for completed units must not exceed $50,000 for Metropolitan Toronto and Northern Ontario, north of the French River and $42,000 for the rest of the province. (These cost ceilings may be revised periodically.)

Up to twenty-five per cent of the units are to be offered for use by the local housing authority responsible for managing assisted housing in the community. In appropriate cases, up to five per cent of the units in the building should be made accessible to physically-disabled persons. First-year rents are negotiated with the Ministry.

To be eligible for the program, work on a project cannot begin prior to the loan commitment. (The land or building may be purchased and a building permit obtained.) Except for senior citizen projects, adults-only buildings are not eligible. Non-profit and cooperative housing may be eligible if NHA assistance were not used. Other government funded projects will generally be ineligible. Projects may be of mixed use and tenure.

Program: Ontario Renews - Adding Rental Units to Existing Housing

Date Started: August 1983

Date Ended: Still Operational

Enabling Legislation: Nil

Administered by: Ontario Ministry of Municipal Affairs and Housing

Objective: An experimental pilot project to create 150 new rental units in existing single-family housing

Description: The pilot projects are located in Toronto, Hamilton, Ottawa and Thunder Bay -- communities which have low rental vacancy rates and large existing housing stock feasible for conversions.

Homeowners interested in a conversion must own and live in the house. Initial applications must be made to the municipality in which the single-family housing is located and conversions must comply with existing zoning by-laws.

The province will provide an average interest-free loan of $7,000 per new unit (secured by a provincially-held mortgage) to underwrite a portion of the selected homeowner's capital costs of converting to provide at least one new legal unit. The loan is interest-free for 15 years. If a unit is "deconverted", the loan will become due and payable immediately.

Program: Municipal Incentive Grants Program

Date Started: 1975

Date Ended: 1978

Enabling Legislation: Fed.: National Housing Act, Section 56.2
Prov.: Federal/provincial agreement, April 1976

Administered by: Ontario Ministry of Housing, Community Planning Advisory Branch; Canada Mortgage and Housing Corporation; municipalities

Objective: To encourage municipalities to permit and facilitate development of medium-density housing of moderate size and price

Description: Municipalities are offered a grant of $1000 by CMHC for each new dwelling unit meeting certain density and size requirements and priced below the limit set for AHOP in that area. The dwellings can be for rent or sale and must be connected to municipal services.

Program: Community Sponsored Housing Program

Date Started: 1974

Date Ended: December 1978

Enabling Legislation: Nil

Administered by: Ministry of Municipal Affairs and Housing and Ontario Housing Corporation

Objective: To provide additional assistance to non-profit housing corporations in housing low and moderate income households and to establish another method of integrating public housing units into the community.

Description: In addition to federal assistance available to non-profit groups, a provincial rent reduction grant is available if units are made available to households eligible for rent supplement. The grant is paid over a 15-year period on a declining scale. The usual rent reduction is $20 to $35 per unit a month in the first year. The rent supplement is also available.

In 1974, the province allocated $4 million in funds for this program.

Program: Ontario Community Housing Assistance Program [OCHAP]

Date Started: March 1981

Date Ended: Still operational

Enabling Legislation: Housing Development Act

Administered by: Ontario Housing Corporation, for Ministry of Municipal Affairs and Housing

Objective: To assist in the provision of rent-geared-to-income housing for individuals and families of low income.

Description: Projects developed with federal assistance under Section 56.1 of the National Housing Act; since August 1, 1978, under the federal private non-profit housing program; and since January 1, 1979, under the non-profit cooperative housing program are eligible. This program operates in conjunction with the Rent Supplement Program, in which the province will provide a 100 per cent subsidy on additional units designated for geared-to-income occupants. Like the Rent Supplement Program, these additional units are made available to low income families and senior citizens on a rent-geared-to-income basis. Tenants pay their portion of the agreed-upon rent directly to the landlord. The difference between the reduced rent and the market rent is paid to the landlord by the Ontario Housing Corporation. Initial OCHAP agreements between the ministry and private non-profit/cooperative corporations cover periods of up to three years. Up to 35 per cent (+5 per cent for the handicapped) of units can be included in family projects and 50 per cent in projects for senior citizens.

At least 50 per cent of the units made available under OCHAP must be offered to the local housing authority which may refer applicants from its waiting list for geared-to-income housing. Provincial OCHAP assistance given in any project will not exceed federal funding.

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CHAPTER 2: CLASSIFICATION OF RENTAL HOUSING POLICIES

1.0 Introduction

The analysis of Chapter 1 of this study showed the numerous and varied approaches to housing policy that have been used by the federal government and the government of Ontario. Any attempt to examine these policies comprehensively, policy by policy, would become bogged down quickly in a morass of detail. Such an unfortunate outcome can be overcome by recognizing that many of these policies share common elements. Thus, a variety of "generic" types of rental housing policies can be distinguished according to the general channels and mechanisms through which they are expected to have an impact. Within the generic classes, differences exist with respect to the details of policies so as to create some differences in their effects on the workings of housing markets. Still, the analysis can proceed by examining the generic types and noting the differences within types only where necessary.

2.0 Market and Non-Market Allocation

In Canada, the market is the predominant mechanism used for determining the allocation of rental housing in our economy. The term "rental", in itself, conveys the sense of a market transaction. To appreciate the role of the market in the allocation of rental housing, it is useful to consider the features of the conceptual alternative, a non-market system of allocation such as exists in the Soviet Union. In such a system, decisions with respect to the volume, quality, location and allocation of housing are determined independently of peoples' willingness or ability to pay. People are assigned to housing and find it difficult to improve their housing by spending more even if they so desired. Similarly, they may be unable to accept housing of lower quality and use the resources saved for any other component of their consumption.

Non-Market allocation. Some indication of the procedures used for the allocation of housing by non-market means can be gained from Di Maio's (1974) study of Soviet housing policy. He describes the procedure of making an application for housing as follows:

> The main concern of the person in need of housing is to get his name put on the waiting list for housing.... The individual seeking better living conditions starts out by filing an application with his local housing operations' office. Attached to his application is a copy of his certificate of occupancy which describes his current housing: its size, number of rooms, whether it is an individual apartment or shared, the number of persons occupying it. If the person is seeking space in a building owned by his work organization he must also provide his personal file.... From the housing operations' office, papers are sent to the appropriate city agency or waiting lists for redistribution of living space.... A 1968 union law stipulates that applications...must be examined within one month. The leadership of the [local unit]...may extend the period for deciding on an application by one more month. Only a decision of the [local unit]...can put a person's name on a waiting list.... The need for housing or for an improvement in housing must be clearly shown.... Because of the housing shortage, thorough verification of the applicant's present housing condition is a necessity. Several official, semi-official and semi-voluntary organizations participate in investigating the petitioner's situation. (pp. 118-119)

Placement on the waiting list is only the first step toward obtaining housing. Di Maio continues:

> ...Soviet legal writers stress the fact that once citizens are on waiting lists, they are assigned living space strictly on the basis of their turn, unless special restrictions apply to them. (p. 119)

A non-market system of allocation is often compared favourably to a market system because it allocates housing on a more equitable basis than ability to pay. Di Maio's evidence suggests priviledged workers get special treatment:

> The more important enterprises, however, have been known to exert pressure to improve an employee's position on the city-wide waiting list. Party membership or position may also influence the outcome of housing decisions. Housing agencies are often in poor circumstances to resist Party suggestions.... The allocation process once again points out the contradiction between a policy which views housing as a public service and a right of our citizens and at the same time ties housing to the rewards system. (p. 119)
>
> The length of his wait and the size of the alloted housing space will depend on several factors in addition to his need, work and social record. If the apartment hunter belongs to a privileged category he will be entitled to special consideration on the priority list or to extra housing space... The additional housing assigned may consist of a separate room, regardless of size. If a separate room is not available, the norm for additional space is ten square meters or where indicated by law, twenty square meters (for example, creative artists and scientific artists).... This additional housing is subject to the same rent level as basic housing space. (pp. 122-23)

While the procedures for obtaining housing may vary according to the place of residence and other characteristics, this description makes it clear that housing is allocated in the U.S.S.R. by a mechanism which is distinctly different from the market mechanisms.

In Canada, a portion of rental housing is allocated by a similar mechanism to that used in the Soviet Union. In particular, public housing is allocated on a basis other than ability to pay. Its allocation manifests many of the same features as the non-market system of the Soviet Union such as complicated application procedures, points systems to determine priority and lengthy waiting lists. Nevertheless, despite the presence of a non-market sector, the market mechanism provides the predominant mechanism for the allocation of rental housing in Canada. As a consequence, the analysis in this study proceeds by examining the consequences of different policies in terms of their effects on the working of the market for rental housing.

3.0 Types of Housing Policies

The scope of the term "rental housing policy" must be delineated for the purpose of this study. One approach would define rental policy narrowly as a policy consciously directed toward some dimension of rental housing or alternatively, a policy with the primary purpose of altering the quality or quantity of housing occupied by renters. Both these approaches are rejected for present purposes. Stanbury (1984a) shows that the public choice analysis of policy makes it very difficult to identify either the conscious direction of policy or its primary purpose. Policy, rather, emanates from a coalition of interests, each of which may have distinctly different motives for wishing a policy enacted. The stated purpose of a policy may be designed so as to make a policy potentially attractive to the general public even though that purpose need not correspond to the objectives of any party in the coalition and, indeed, may not be descriptive of the effects of the policy.

The use of the term "rental policy" for present purposes will avoid the need to identify the motive or purpose of any policy. A policy will be identified as a rental policy to the extent that it influences or affects the quantity or quality of the rental housing available to households and individuals. This approach should be less ambiguous than the alternative because, conceptually, it is easier to determine whether a policy affects housing than it is to determine the intent or purpose of the policy.

As stated in the introduction and earlier in this chapter, the numerous variants of housing policy make a policy-by-policy review unfeasible. The mass of detail would obscure any generalizations about the effects of different types of policy. Fortunately, the dimensions of the differences among policies are simpler than a superficial review would suggest. For present purposes, rental housing policies can be classified according to their inital impact on the housing market.

Four "generic" types of rental housing are distinguished:

1) Market augmenting policies work through influencing the behaviour of private market participants (i.e., tenants or private landlords or both) under a given set of market conditions and institutions.

2) Market replacing policies work through influencing some third party other than private landlords (i.e., either government, its agencies, or non-profit participants in the housing market) to supply rental housing.

3) Rent regulating policies serve to alter the market outcome from that which would have occurred, given the existing demand from tenants and existing supply from landlords.

4) Institutional policies alter the arrangements which govern the actions of market participation in either

the supply of housing or in the terms of transactions between tenants and landlords.

Each of these approaches will be discussed more fully below in order to make the distinctions among them clear.

3.1 Budgetary Versus Non-Budgetary Policies

This four-fold classification of rental housing policies tends to mask another essential difference among policies. Market augmenting and market replacing policies can both be characterized as budgetary policies in that they require changes in government expenditures or tax revenues in order to alter market outcomes. These policies require the government to change the incentives of market participants by changing either the subsidies that they receive or the taxes that they pay when they carry out certain actions which affect the demand or supply of rental housing. Market replacing policies require the government either to make direct expenditures itself or to make subsidies to non-profit participants. In contrast, market regulating and institutional policies can be classed as non-budgetary policies in that neither depends on the effects of direct government expenditures or taxation to achieve its effect. Market regulating policies constrain the outcomes of market processes in order to achieve their effects, whereas, institutional policies change the sets of allowable behaviour for market participants.

This classification between budgetary and non-budgetary policies may be misleading in an important respect. It may leave the impression that budgetary policies are costly whereas non-budgetary policies are not. Such an impression, however, is totally misleading but its source is easily understood. Budgetary policies, especially market replacing and demand augmenting policies, require government to make direct expenditures which must be financed by revenues. For some other budgetary policies, the costs to the government's budget are more subtle. Some supply augmenting policies work through the foregoing of tax revenues to encourage the desired activities. The recognition that foregone tax revenues are as much a cost to government as direct expenditures has been made explicit by the use of the term "tax expenditure" to describe programs that work through the incentive of reduced taxes. Non-budgetary policies have the apparent appeal to some that they can meet their objectives costlessly -- such an impression could not be farther from the truth. The essential difference between budgetary and non-budgetary policies is that the costs of the latter are less visible and do not show up on the government's budget directly. Rather, these costs appear through an impairment in the workings of the market mechanism in which costs are placed on one or the other of the market participants. Rent regulation, for example, can, in the first instance, be regarded as a tax upon landlords. Like any other tax, its final incidence may not be the same as its initial impact. The costs may be spread from landlords to tenants, potential tenants and even taxpayers at large. Many budgetary policies, including those in the housing area, are a response to the impairment of the workings of the market produced by the use of non-budgetary policies. The reader should note, for example, the proliferation of budgetary policies for rental housing, documented in Chapter 1, that followed the introduction of rent regulation, a non-budgetary policy, in 1975.

3.2 The Workings of Market Augmenting Policies

Market augmenting policies can be identified by the fact that they work through altering the behaviour of private participants in the rental market by increasing their willingness to demand or supply rental housing in face of any given set of incentives or signals emanating from that market. This definition has several separate elements. First, the policy works by influencing the behaviour of market participants. Second, it either alters their willingness to be suppliers of rental housing or influences their cost or opportunities for housing as consumers under a given set of rents or prices which exist in the the market.(1)

The first criterion assures that market augmenting policies do, in fact, augment rather than supplant the market by ensuring that the policies work through influencing the behaviour of the participants who would be in the housing market in the absence of government policies.(2) The second criteria ensures the policy augments the market by working through the same devices which would produce the market outcome in the absence of regulation. This test also prevents the classification of rent regulation of any form as a market augmenting policy. Even though rent regulation serves to alter the behaviour of market participants, it does so by constraining them from acting in response to the forces which would be generated by the workings of the market.

The definition of a market augmenting policy is intended to describe the mechanism through which such a policy creates its effects but not to place any limitation on the environment other than that it be a market setting. The importance of this observation is two-fold. It emphasizes again that a market augmenting policy influences the behaviour of private demanders and suppliers of rental services in carrying out their market transactions. In addition, the definition does not rule out the presence of other governmental influences in the market. The level of rents faced by demanders and suppliers could be determined by some form of rent regulation. Although rent regulation in itself would not be classed as a market augmenting policy, a complementary policy which alters the market behaviour of private demanders and private suppliers of housing, in face of a regulated level of rents, would be a market augmenting policy.

An example can be used to show the overlap between market augmenting and rent regulation policies. Consider a policy of rent regulation which succeeds in holding market rents substantially below the levels which would prevail in its absence. In time, it may become apparent that this policy of rent regulation inhibits the supply of rental housing, bringing forward a call to government to do something about the shortage of rental housing. Introduction of tax concessions or direct subsidies may succeed in increasing the supply of rental housing in these circumstances. Note that what was initially a non-budgetary policy to keep rents down has triggered a budgetary response. The "tax" on landlords resulting from the rent regulation has been replaced by a subsidy from the public purse.

The basic definition of rental policy presented earlier stressed the importance of the effects of a policy as distinct from the intent or proclaimed purpose in determining whether a policy should be classed as a rental policy. In considering the effects of market augmenting policies, a further distinction should be made between the proximate and indirect effects. In part, these policies work by altering directly the behaviour of market participants in face of a given set of market conditions. This effect can be characterized as the proximate or direct effect in that the policy directly shaped the conditions determining that economic actors' behavior. The influence of the policy, however, extends beyond this proximate effect. The change in behavior caused by the proximate effect may alter market conditions in such a way that the incentives for other economic actors are also changed. Any actions which are taken in response to this changed incentive can be characterized as induced or indirect effects.

An evaluation of the effects of housing policies must distinguish clearly between the proximate and induced effects of the policy. A policy may have the same proximate effects in different circumstances but substantially different induced effects so as to alter the overall outcome. For example, a housing allowance program may raise the incomes of certain groups of households so that they desire to spend greater amounts on housing. The proximate effect can be described as a greater demand for housing. The induced effects depend on the other characteristics of the market and would, for example, be influenced by the degree of tightness of the market. In a tight housing market, the greater demand for housing might induce higher rent levels, whereas, in an easier housing market it would lead to a reduction of the vacancy rate in the short run.

Market augmenting policies differ according to whether their proximate effect influences the demand or the supply side of the rental market. Market augmenting policies on the demand side work through influencing the demands of households for housing, whereas, supply policies work by influencing property owners or developers to increase the supply of rental accommodation. A wide variety of specific policies and programs are covered under these classifications.

4.0 Demand Augmenting Policies

The definition of demand augmenting policies encompasses a wide range of policies. At one extreme, it includes general policies of income distribution which influence recipient households' demands for housing and for other goods, through affecting their overall income. Negative income taxes, welfare payments, and even unrestricted housing allowances fall into this category of policy. Less obvious, but still relevant are policies directed towards supporting the consumption of other goods or services. For example, a food stamp program may leave recipient households with more discretionary income to spend for housing if their consumption of food products increases by less than the value of food stamps.

An unrestricted housing allowance differs from other general redistributive policies only in terms of the determination of the benefit received by the target groups. Typically, the benefit to a household from such a program is defined in terms of the difference between the household's income and the cost of some standard of housing, appropriate to the size, age, and other characteristics of the household. While the household's level of support may be set by the standard expense for housing, the household is not required to meet any spending level for housing in order to qualify for the allowance.

The general policies contrast with restricted housing allowances, which make the benefits dependent on the recipient meeting specified housing standards. Either physical standards or standards based on spending on housing services, whether in absolute value or percentage of household income, may be used to establish eligibility for income transfers.

The demand augmenting policies that have been discussed to this point apply equally well to rental housing and owner-occupied housing.(3) In addition, there are several types of policies which can be used to stimulate demand for owner-occupied housing which lack any parallels as stimulants to the demand for rental housing. Policies which subsidize home mortgages reduce the costs to households of home ownership relative to renting. Similarly, a variety of government programs have provided grants to new home owners. Finally the Registered Home Ownership Savings Program (RHOSP), though now discontinued, provided delay and eventual forgiveness of taxes, if the proceeds are used to purchase a house.

5.0 Supply Augmenting Policies

Supply augmenting policies consist of those policies which alter the availability of housing by influencing decisions of suppliers such as landlords and developers. At a most general level, any policy which creates a favourable policy for investment, in general, is likely also to be favourable to investment directed toward housing. Low real interest rates and low corporate taxation, whether through favourable depreciation allowances or low tax rates, would both be conducive to investment in general.

Supply augmenting subsidies, specific to housing, can be directed at any of the stages of bringing housing to the market. For example, subsidies designed to reduce the cost of supplying housing could be directed toward either lowering the costs of land acquisition or reducing the costs of constructing rental housing. Both these types of subsidies could be used to encourage both renter and owner-occupied housing. On the other hand, policies which subsidize the continuing costs of housing are more suitable for rental housing than for home ownership. This type of subsidy could be in the form of a supplement to a landlord's rental revenues received from tenants. A final type of subsidy for rental housing results from joint ventures between private and government enterprises for the supply of housing. A subsidy occurs if the return on the government's investment from the enterprise falls short of the returns that the same funds could earn in alternative uses.

Some of the subsidy programs aimed at augmenting supply are difficult to distinguish from subsidy programs which augment demand. A landlord might be subsidized $X per month for renting accommodation to a particular tenant or alternatively, the tenant might receive a $X per month subsidy for occupying the unit rented by the landlord. With suitable constraints on the behaviour of the landlord or tenant, these programs could be made to be equivalent. The difference in classification reflects only the fact that the basis for the present classification is the proximate effect of the policy.

The tax system provides another channel through which housing policy can be implemented. Like the subsidy program, the tax incentives for housing can affect different stages of the supply process for housing. Exemptions from sales tax on construction materials reduce the cost of purchasing housing units for landlords and homeowners. Accelerated depreciation, in contrast, would increase the return to the landlord by lowering the taxes payable out of current revenues.

A further supply augmenting approach to rental housing consists of concessionary mortgage terms. At one level, subsidized terms for mortgages are little different from other forms of subsidy in that they reduce the expenses for the landlord. Nevertheless, the decision to finance differs from the decision to invest in rental housing. For this reason, subsidized interest rates on mortgages are distinct from other government subsidy programs in housing.

6.0 Market Replacing Policies

Market replacing policies, as already stated, operate through influencing third parties to make rental housing available. A basic distinction between supply augmenting and market replacing policies reflects the nature of the supplier. Supply augmenting policies are aimed at altering the incentives of private landlords to make rental housing available. Market replacing policies depend on suppliers whose primary motive is something other than the return on investment. These suppliers include the government itself and its agencies. In addition, part of the non-profit or "third" sector can be included as suppliers through which market replacing policies can be expected to operate.

A distinction can also be made with respect to the motives through which supply augmenting and market replacing policies work. Supply augmenting policies work by enhancing the suppliers' expected rates of return at any level of market rent. In contrast, market replacing policies are motivated by factors other than gaining a profit from investment. Governments and their agencies bypass the market by supplying housing directly to individuals and families for the purpose of achieving social objectives such as those to be discussed in Chapter 3. Similarly non-profit organizations supply housing for motives such as service to others, rather than for profit.(4) This difference, however, can be exaggerated. Just as the prospect of inadequate profits can discourage the private landlord, so too, the prospect of large losses can discourage the non-profit governmental supplier.

7.0 Rent Regulating Policies

Rent regulating policies serve to alter the market outcome from that which would have occurred, given the existing demand from actual or potential tenants and existing supply from actual or potential landlords. In effect, some set of rules or the decision of a government agent limits the workings of market supply and demand to some acceptable or allowable outcome. Much economic evidence documents the way in which an attempt to control some dimensions of the market outcome tends to produce unintended effects in other dimensions. In particular, the regulation of market rents in the housing market may produce a deterioration in quality of existing rental units and a decreased flow of new rental accommodation, other things being equal.(5)

Rent regulation of market outcomes has proved to be a popular instrument of housing policy, in the sense of being adopted over widespread jurisdictions. Moreover, since its adoption in 1975, it has been a major instrument shaping the rental housing market in Ontario. As Stanbury and Vertinsky (1985) point out, about 830,000 tenant households in Ontario "have a direct experience with and a direct stake in rent control" (p. 1.1).

Part of the appeal of rent regulation appears to be based on the illusion that these policies are costless. The earlier discussion in Section 3.1 above should have dispelled this illusion. Rent regulation differs from other housing policies in that its costs are non-budgetary rather than budgetary. This difference may appeal to certain interest groups, to the extent that the degree of public scrutiny may be less for non-budgetary policies because of the greater difficulty in assessing the costs of providing benefits to this group.(6) Nevertheless, the costs of achieving social objectives through rent regulation are likely to be as great, if not greater, than through budgetary policies.

The presence of rent regulation must be clearly recognized in any study of the workings of the rental housing market in Ontario and was the direct impetus for this study of the rental housing market. The Commission of Inquiry into

Residential Tenancies has among its terms of reference the task

> to recommend what measures, in addition to rent review, the Province of Ontario might take to assist in providing rental accommodation at fair rents....

This present study is directly concerned with the policies which are complementary to rent regulation and can be used to achieve the goals of rental housing policy. It is recognized that these alternatives to rent regulation may involve substantial budgetary costs to government. Nevertheless, rent regulation, as Stanbury and Vertinsky (1985) show, may be a very costly means for realizing social objectives. This study provides a basis by which the costs of using alternative policies to replace or supplement rent regulation can be compared with each other and with the costs of rent regulation itself.

8.0 Institutional Policies

For the sake of completeness, one set of policies is discussed here that will not be subject to more detailed scrutiny in the remainder of this study. Institutional policies establish the ground rules under which housing can be supplied. They consist of the set of rules which delineate acceptable or legal forms of behaviour by suppliers from unacceptable or illegal in all dimensions except rent. These rules govern who is permitted to participate in the market, what products or services can be supplied and the conditions under which they can be supplied. To some degree, these rules resemble the market regulating policies discussed above. They are discussed here because, like rent regulation, they shape the ultimate market outcome.

For the housing market, two major types of institutional policies can be distinguished:

1) those governing the relationship between landlords and tenants,

2) those which limit the types of rental housing supplied on the market.

The dimensions of the landlord-tenant relationship governed by institutional policies include the terms of eviction, the frequency of changes of rent, the information requirements imposed on the participants and other rights and obligations of landlords and tenants. Any movement toward changes in tenant-landlord relationship through the establishment of a housing ombudsman, the location of special housing courts or the regulation of collective bargaining rights for tenants (Reid, 1984), would represent a major change in the institutional structure of the rental housing market.

Institutional policies can affect the availability and cost of rental housing in a variety of ways. Zoning by-laws, minimum standards for construction embodied in building codes, union and trade legislation and lengthy planning and approval processes, all add to the cost of supplying rental housing and influence the availability of housing at any level of rent.

A detailed examination of institutional policies in the rental housing market is beyond the scope of the present paper. Yet, it is clear that these policies shape the performance of the rental housing markets in a fundamental way. A number of questions should be raised regarding these policies because of their interaction with the policies under review in this study:

- what is the purpose of existing institutional constraints?
- what are their costs and benefits?
- who benefits and who loses from these rules?

8.1 The Purpose of Construction Standards and Land Use Controls

The regulations governing land use and construction have been justified on the grounds that they prevent people from having to live in unpleasant environments or in substandard housing. Yet, if these policies are aimed at protecting the occupants of the housing, it must be assumed that they are uninformed or unable to make choices on their own.(7) On the other hand, the motive behind these measures may be, instead, to protect others from the intrusion of lower cost housing into their neighbourhoods. Dahlman (1982), for example, concludes in his study of the effects of zoning law that:

> ...zoning by-laws have become the tool by which the members of a residential district protect their investments and lifestyles. (p. 252)

8.2 The Costs of Construction Standards and Land Use Controls

Building codes and zoning by-laws impose costs by making housing more expensive than it would be in its absence. The evidence available for Canada on these costs is very limited. Marks (1984), in his study for the Commission, reports on American evidence gathered by Seidel (1978). Table 2.1

presents Seidel's list of government regulations classified according to the component of housing cost which they affect. Seidel also estimated the unnecessary costs for different types of regulations, as presented in Table 2.2. On the basis of these data, Seidel concludes:

> Contrary to previous surveys in past years, government regulations were now considered to be the primary problem in doing business. (p. 38)

8.3 The Distribution of Costs and Benefits

Zoning by-laws and construction codes apply equally to all homebuilders. This does not mean that their costs are equal across all households. Families and individuals, which would have planned to occupy housing of a quality equal to or in excess of the standards, do not have to bear any unnecessary costs except for the costs of verification. Indeed, they may benefit to the extent that they can be assured that their neighbourhoods are composed of similar quality housing. The costs of these regulations are borne directly by those households that would have chosen lower quality housing than permitted by the standards. In order to occupy legal housing, they are required to pay more than they would have chosen without the regulations. In general, these households affected by the requirements will be lower income households. Thus Dahlman (1982) concludes:

> The perhaps most central gainer from the use of zoning in a community is the relatively wealthy single-family homeowner.... The losers have been the poorer people who have not been able to make their demands for cheaper housing effective in the marketplace, due to the artificial controls imposed on the price system as an allocator of land. In effect, zoning has become a tool for redistributing income from the poor to the rich.... (p. 253)

TABLE 2.1

Government Regulation Affecting the Cost of Housing in the United States

	Housing Cost Component Affected					
Level, Type of Regulation	Unimproved Lot	Land Development	Land Development Financing	Structural Materials and Labour	Construction Financing	Mortgage Financing & Settlement Costs
Federal government						
Clear Air Act	x					
Coastal Zone Management Act	x	x	x			
Consumer Product Safety Act				x	x	
Federal Noise Control Act				x		
Federal Water Pollution Control Act	x	x	x			
FHA and VA Mortgage Programs				x	x	x
National Flood Insurance Programs	x	x	x	x	x	
Occupational Health and Safety Act			x	x		
Real Estate Settlement Procedures Act			x	x	x	
State government						
Building codes				x	x	
Coastal zone management	x	x	x			
Critical areas restrictions	x	x	x			
Land development acts	x	x	x			
Sewer moratoria	x	x	x			
Local government						
Bonding requirements		x				
Building codes				x	x	
Energy codes				x	x	
Engineering inspection		x	x	x		
Environmental impact review	x	x	x			
Mechanical codes				x	x	
Plant review		x	x			
Sewer connection approval and fee		x	x			
Shade tree permits		x	x			
Site plan review		x	x			
Soil disturbance testing		x	x			
Utility connection fees		x	x			
Water connection approval and fee		x	x			
Zoning	x	x	x			

SOURCE: from Marks (1984), p. 94. Seidel, 1978, Exhibit 2.10, p. 20.

TABLE 2.2

Unnecessary Costs of Regulation, United States

Level, Type of Regulation	No Increase (less than 1%)	Significant Increase (1 - 5%)	Very Significant Increase (more than 5%)	Total*
Building Codes	26.7	39.8	33.6	100.0
Coastal zone regulations	76.0	8.1	16.0	100.0
Energy coes	50.2	31.0	18.9	100.0
Environment impact statements	38.3	26.0	35.7	100.0
Floodplain protection	54.5	20.5	25.0	100.0
Mortgage finance requirements	30.1	40.4	29.5	100.0
State land development laws	44.2	23.2	32.6	100.0
Settlement costs	36.8	34.3	28.8	100.0
Subdivision requirements	7.6	20.3	72.1	100.0
Zoning	39.7	24.1	36.3	100.0

* May not add to 100.0 due to rounding.
N = 2471

SOURCE: from Marks (1984), p. 95. Survey of the Home Building Industry, Center for Urban Policy Research, Summer, 1976. Seidel, 1978. Exhibit 3.15, p. 38.

In a similar vein, Marks (1984) declares:

> A recent study of the Oshawa - Whitby area suggests that the affordability problem there has been aggravatedby local regulations andstandards.(p. 93)

A comprehensive review of the effects of zoning and other regulations is beyond the scope of this study. Nevertheless, these local policies are part of the environment in which provincial and federal policies must operate. By affecting the cost and supply of housing, they also influence both the need for and the cost of policies carried out by other levels of government. The provincial government should be aware that the costliness of its programs may be affected materially by the choices made by local government. As been noted elsewhere in this study, existing policy of all levels of government may contribute to the problems toward which housing policies are directed.

9.0 The Classification in Action

As stated before, the purpose of the classification developed in this chapter is to establish representative, "generic" types of policies which can be analyzed with respect to the effects from pursuing these policies on the goals of housing. Thus, the classification focusses on the conceptual features of the policies most germane to their influence on the housing objectives. From a practical perspective, this approach raises several questions. Can the classification distinguish among policies clearly? Which real-world policies fit the conceptual categories?

Table 2.3 provides an answer to these questions. It classifies each of the federal and provincial policies which were described in the appendix to Chapter 1, on the basis of the included description. As can be seen, none of the policies described would be classified as demand augmenting whereas, a large number of both supply augmenting and market replacing policies were identified. Several policies had a variety of options built into them which made it possible for them to fit more than one classification.

The basis for classification may be seen by considering two examples:

1) Limited dividend housing program (Federal)-Supply Augmenting: This program is considered as supply augmenting because it encouraged building owners to develop "moderately priced rental accommodation". The incentive to private developers was a 95 per cent loan at a "below market" rate of interest. The essential element which makes this program supply augmenting is the fact that it works through private owners.
2) Municipal Non-Profit Housing Program (Provincial) - Market Replacing: This program is similar to the limited dividend program described above in that it subsidizes the costs of supplying rental housing. It is classed as market replacing, however, because it provides assistance only to municipally owned non-profit housing corporations.

This chapter has developed a system of classification which can be used to analyze the workings of housing policy. Before the system can be used, a set of criteria must be established for assessing housing policies. This is the task of the next chapter.

TABLE 2.3

The Classification of Federal and Provincial Rental Housing Programs

1. Demand augmenting

    none identified in Ontario

2. Supply augmenting

    Federal:
    - Limited Dividend Housing Program
    - Insured Loans
    - Mortgage Insurance
    - Federal/Provincial Rural and Native Housing
    - Residential Rehabilitative Assistance Plan (RRAP)
    - Multiple Unit Residential Buildings (MURB)
    - Assisted Rental Program (ARP)
    - Graduated Payment Mortgage (GPM)
    - Canada Rental Supply Plan (CRSP)
    - Municipal Incentive Grants (or market replacing)

    Provincial
    - Rent Supplement Program
    - Accelerated Family Rental Housing Program
    - Private Assisted Rental Program
    - Ontario Rental Construction Grant (ORCG)
    - Ontario Rental Construction Loan Progam (ORCL)
    - REnt HAB/Demonstration Projects
    - Innovative Rental Construction Loan Program
    - Neighbourhood Improvement Program (NIP)
    - Convert-to-Rent
    - Ontario Renews - adding Rental Units to Existing Housing
    - Municipal Incentive Grants Program (or market replacing)
    - Elderly Persons Housing Aid Act (or market replacing)

3. Market Replacing

    Federal
    - Public Housing
    - Non-Profit Cooperative Housing Assistance Program (CMHC, Section 56.1, Non-Profit and Cooperative Housing Program which replaced Section 15.1 and 34.18 programs)
    - Community Resource Organization Program (CROP)
    - Department of Veterans Affairs Housing Program for Veterans (loans for low rental housing projects to non-profit group)
    - Municipal Incentive Grants (or supply augmenting)

Table 2.3 (cont'd)

Provincial

- Elderly Persons Housing Aid Act (or supply augmenting)
- Student Housing
- Municipal Non-Profit Housing Program
- Northern Ontario Assistance in Housing
- Wigamen Incorporated
- Community Sponsored Housing Program
- Ontario Community Housing Assistance Program
- Municipal Incentive Grants (or market replacing)

Notes to Chapter 2

(1) It should be noted that this definition does not specify whether the signals come out of a controlled or uncontrolled market. Rather, it requires only that the signals are those which face market participants and those to which they react.

(2) Not all would rent in absence of government policies because the level of rents may be high enough to ration them out. All would be potential renters in that they would rent if the level of rent were low enough.

(3) Rental housing policies, as discussed in Chapter 1, also affect ownership decisions, and vice versa. If housing policies increase ownership demand, they reduce rental demand as a consequence.

(4) A distinction must be made between different elements of the third sector. Most non-profit housing carried on by public bodies or private non-profit organizations does not benefit the initiators, either through the receipt of profits or through the receipt of housing on favourable terms. The exception is cooperative housing. Many of those individuals who assist in planning and implementing cooperative housing projects will ultimately benefit through gaining housing on favourable terms. Despite the recognition of this difference between cooperative housing and other non-profit housing, they will be considered together in this study to confirm with the treatment given in most background material.

(5) See Arnott (1981) and Stanbury and Vertinsky (1985).

(6) See Lermer and Stanbury (1985) for a more complete discussion of this point.

(7) This issue is discussed in more depth with respect to the affordability and housing goal in Chapter 3.

CHAPTER 3: EVALUATION CRITERIA FOR RENTAL HOUSING POLICIES

1.0 Introduction

As discussed in Chapter 1, any evaluation of the workings of housing policy can only be made from the perspective of the goals to which it is directed. Yet from the standpoint of the evaluator, these goals are rarely clear. The formulation and implementation of any policy requires the support of a variety of different interests, each of which may have different reasons for giving their support. Moreover, as Stanbury (1984b) has shown, the presence of a policy creates a whole new set of interests. Thus, the reasons for supporting a policy, once it is implemented, may differ substantially from those that led to it.

Chapter 1 provides an initial discussion of the criteria which will be used in this study to evaluate the workings of rental housing policies. The purpose of this chapter is to develop, more fully, the set of criteria to be used in this study.

In an earlier study, Stanbury (1984a) discussed with insight the normative judgements which can be used as support for rent regulation. He has classified the arguments for rent regulation into three categories:

> 1. Actions by government designed to alter the distribution of income, wealth or consumption opportunities.
>
>   a) To prevent rent "gouging" or "unconscionable" increases in rent so as to prevent landlords from obtaining "exorbitant" profits or "unearned windfall gains. "
>   b) To maintain or increase the amount of "affordable" rental housing for households with low incomes....

2. Actions by government to create certain rights and thereby remove certain things from the market exchange process.

   a) To provide security of tenure for tenants as a right independently of rent control or as a complement to such controls....

3. Actions by government to improve the efficiency with which society's scarce resources are allocated.

   a) To remedy certain problems in rental housing markets said to be market failures, e.g., imperfect information and high transaction costs.
   b) To stabilize the adjustment path of rents in disequilibrium situations in the rental housing market in order to reduce the economic costs of the process of adjustment. (Stanbury, 1984a, pp. 1.2-1.3)

Subsequently, Stanbury (1984b) has also discussed a further objective which has been used to justify rent regulation: the need to ensure diversity and balance. In summary, Stanbury's criteria for rent regulation can be stated as:

1) to prevent rent gouging,
2) to maintain or increase affordable housing,
3) to provide security of tenure,
4) to reduce market failure,
5) to stabilize the adjustment path of rents,
6) to ensure diversity and balance.

2.0 Framework for Policy Evaluation

This study evaluates a set of housing policies, complementary to rent regulation. In general, these policies are intended to achieve many of the same goals as rent regulation. Thus, the criteria established by Stanbury for the evaluation of rent regulation can provide a starting point for the evaluation of complementary housing policies.

Nevertheless, the criteria used in this study must go beyond those used for assessment of rent regulation by Stanbury for a number of reasons.

2.1 Constraints on Policy

First, the criteria are used in this study for a different purpose than that of Stanbury. He states:

> We focus on the arguments made in support of some type of rent regulation: why such regulation ought to be introduced, retained or modified to make it more effective from the point of view of its proponents. These arguments, by definition, are based on value judgements. (Stanbury, 1984a, 1-1)

The arguments examined by Stanbury can, in some sense, be equated to the concept of the preference framework used in economics. It characterizes the tastes of consumers or, in this case, of advocates of rent regulation. Choice, however involves more than tastes. Constraints limit the degree to which we can fulfill our tastes. In the case of a consumer, the constraint is spending power as determined by income. In the case of the policy maker the constraint may be the resources available for carrying out policies to different ends.

This difference between constraints and tastes can be made clear by example. Many of us say we prefer Ferraris to Chevrolets, champagne to beer and steak to hamburger. Yet, our consumption consists entirely of Chevrolets, beer and hamburger. This inconsistency does not mean we have not described our tastes accurately. On a one-for-one basis, we may always choose champagne over beer. The constraint of limited resources, together with the prices of the two beverages, means we never face this choice. On the basis of the forty beer to one champagne choice that we face we decide to settle for the beer.

A parallel exists in choice of policy. Even though we may prefer a given policy for one purpose, we need to take a broader perspective before choosing it. This broader perspective involves constraints. How does the policy affect other goals? What are the direct costs of implementing the policy?

The evaluation of housing policy faces a dilemma of determining which criteria should be used to assess the working of any set of policies. Moreover, once the choice of criteria has been made, a further choice remains with respect to the weighting to be attached to each. To remain neutral, the evaluator must consider the performance of a policy in terms of any generally accepted criteria and leave the weighting among the criteria up to policy makers. The choice of an appropriate housing policy involves a matching of policies, according to their effects with the objectives most valued by the authorities.

The discussion to this point suggests that constraints must be considered, in addition to normative goals, in assessing the workings of housing policy. As a result, the normative goals described by Stanbury are supplemented by a number of criteria reflecting constraints:

1) effectiveness for cost, and
2) administrative cost.

The need to consider a constraint for the policies considered in this study may appear more urgent because these policies, as shown in Chapter 2, are budgetary policies that require the use of resources by the government carrying them out. This difference, however, is more apparent than real. The impression that non-budgetary policies are not bound by constraints is wholly spurious. As discussed in Chapter 2, this impression may be caused by the fact that the costs of non-budgetary policies are more subtle and less direct than the costs of budgetary policy. The costs of a non-budgetary policy include the detrimental effects with respect to some goals which come about through the pursuit of another. Moreover, regulatory policies impose costs on individuals in just the same way as budgetary policies. The inability to collect a rent because it exceeds a rental ceiling is every bit as much a cost as a tax of equal value. Non-budgetary policies also require an administrative apparatus within government. The requirements of the program also may impose costs to the public in establishing that they conform to the requirements of the program.

Without doubt, the constraints on budgetary policies are unavoidable and obvious. How many resources must the government commit to the program? What are its implications for administrative costs of the government? What does the program buy for each dollar spent?

2.2 Other Dimensions of Evaluation Criteria

Two further matters are relevant for the choice of the evaluation criteria used in this study. First, just as additional criteria were needed for evaluating the complementary housing policies, so too, some of the normative bases for rent regulation may not be suitable for judging other housing policies. In particular, the policies considered in this study can be viewed as most suitable for influencing the housing market over the long run. Part of each policy is directed toward inducing different behaviour than the demander or supplier of housing would make in its absence. These decisions include the choice of residence for households and the decision to invest by landlords. Generally, these decisions are costly to change. Thus, the policies considered in this study are not suitable for carrying out short-term objectives. For this reason, Stanbury's "stabilizing the pattern of adjustment" objective is not applied to the policies under review.

A final criterion which is used in this study should also be introduced at this point. The objective of "feasibility" is used to represent the appeal of the policy to the various interest groups which can influence policymakers in reaching their decisions. This criterion is presented as an antidote to the view that the demonstration of inherent superiority of a policy on the basis of the criteria adopted by the evaluation is sufficient for its adoption once these qualities are proclaimed. The analysis of Trebilcock et. al., Stanbury, and Hartle suggest that more practical matters must be considered. A policy's acceptance depends on the mobilization of support on its behalf from interested parties. Moreover, the implementation of a policy may be dependent on the level of government proposing it and the degree of cooperation among governments that it requires. The feasibility criterion is intended to give indication of the sources of support and the practical difficulties in implementing any policy.

This section has reviewed some of the problems which must be dealt with in establishing the criteria used for the evaluation of policy. We now turn to a more detailed examination of these individual criteria.

3.0 Affordable Housing

Affordability has long been expressed as a major goal of housing policy. As Marks (1984) notes, the Special Parliamentary Committee on Housing stated in its Report of 1935: "The formation, institution and pursuit of a policy of adequate housing should be accepted as a social responsibility."(1) Two elements of this quote should be noted for they served to govern much, but not all, subsequent housing policy. First, the statement clearly establishes the adequacy of housing dimension as a criterion for judgement. Second, and just as important, it proclaims the "formation, institution and pursuit" of housing policy as a social responsibility. This not only suggests that government should pursue this goal, but it also implies it is a responsibility borne by society as a whole. Despite the longevity of affordability as a stated goal of housing policy, this objective must be examined more carefully before establishing criteria for assessing housing policies because the goal is ambiguous and can be interpreted in a variety of ways.

The affordability of housing to any household depends on the relationship between, on the one hand, its income and, on the other, the costs of the desired level of housing, together with the costs of other things it purchases. This relationship shows that affordability of housing can be viewed in two ways: i) as a question of the adequacy of income to purchase suitable housing and ii) as a question of delivering more affordable housing to households at their current income. From the former perspective, affordable housing is a question of adequacy of income and can be pursued by policies designed to redistribute income whereas, in the latter case, affordable housing is, instead, a question of adequacy of housing and can be pursued by policies directed toward the supply of housing.

The contrast between these two approaches to affordable housing should be emphasized. The former approach, focussing on income, would judge a policy which raises incomes and enables people to purchase more and better housing a success, even if the people do not spend more on housing. The target group of households would have the opportunity to purchase better housing but they choose not to. Moreover, their existing housing becomes more affordable in the sense that it absorbs a smaller proportion of their income than previously. In contrast, such a policy would be judged as ineffective by the latter approach because nothing happens to the quality of the housing occupied by the target group. In a nutshell, affordable housing can be viewed as either an income distribution policy or a housing policy.

The fact that the affordability goal encompasses two such diverse elements means that it is impossible to develop a single set of criteria for measuring the success of achieving this goal. The discussion of criteria for each of the dimensions of affordability will be developed separately.

4.0 The Adequacy of Income

Many government policies are directed explicitly toward attaining a "better" distribution of income. The primary policies directed toward income redistribution include the structure and level of the system of taxation, general income transfers such as family allowances and Canada pension payments, and transfers to specific groups such as unemployment insurance and old age security payments. Less clear to most observers but still significant are the income distribution effects of education and resource policy. It is very difficult to imagine any government program which is wholly neutral in its income distribution effects.

If housing policies gain their justification through the redistributive motives of providing affordable housing to lower income groups, the beneficiaries of these policies should be determined. Do the housing policies have the effects on income distribution that were intended? The standard way of approaching this question requires measuring the benefits received from the program by the various income groups in the economy. The results of such an exercise can be judged in terms of the criteria of horizontal equity and vertical equity.

4.1 Horizontal Equity

A widely accepted principle with respect to income redistribution through government taxation and expenditure is that of horizontal equity which states "individuals in similar circumstances should be treated similarly (Buchanan, 100)." The rationale for this principle has been stated by Buchanan (1970):

> Its source is the principle of equality of individuals before the law, tax treatment being legal treatment in essential respects. (p. 100)

Buchanan continues with an observation with relevance to the United States:

> Arbitrary and capricious treatment of individuals by legal institutions is prevented by constitutional law, and this constitutional protection against arbitrary and discriminatory treatment by government has been extended to apply to the distribution of laws. (p. 100)

In Canada, even under the Charter of Rights, it is problematic whether there is any constitutional protection of this nature or scope. The provisions with respect to property rights were deleted from the draft of the Charter before it was brought into force. The extent of protection under the recent equality provisions is uncertain.

Despite the legal uncertainty about the status of horizontal equity, it is a generally accepted value judgement which is applied to assess public policy. While Buchanan has expressed the principle of horizontal equity with respect to taxation only, it applies with equal force to any other government program, whether expenditure or regulation, which affects the distribution of income.

A major problem with the concept of horizontal equity is that it requires the identification of the individuals that are in similar circumstances. No two individuals are likely to be identical in all dimensions. Obviously, any use of the concept of horizontal equity requires some initial agreement as to which dimensions are relevant to the comparisons among individuals.

A further consideration for horizontal equity judgements is the role of the individual's own choice in determining current circumstances. Atkinson (1975) in The Economics of Inequality states:

> Individuals differ in their tastes with regard to work, to saving and to risk taking. As a result, people with the same opportunities may make different decisions, leading to disparities in observed income or wealth. One person may prefer a job with low earnings but short working hours and little responsibility. A person who prefers to save while working to provide for old age may have more wealth when he retires than those who preferred to consume when they were younger. (p. 5)

The aspect of personal choice in determining circumstances complicates further the comparison. If one individual attains a given income at a given age by exerting his productive capacities to the fullest extent and another individual of the same age attains the same income without exertion of his full potential, should the two individuals be considered alike for the purposes of equity comparisons? In other words, is horizontal equity based on an individual's opportunities or their current circumstances? The argument implies no judgement about the need for or the degree to which people use their potential. It simply suggests that commonly used measures may not be enough for making equity judgements.

What significance does horizontal equity play in assessing the performance of government housing programs? Government programs differ with respect to their coverage. Some may offer roughly equal benefits to people in essentially the same circumstances while others are uneven in their incidence, even among similar groups. In some cases, policies by their nature offer relatively large benefits to a limited group of designated recipients. When benefits are not universal with respect to individuals in similar circumstances, some rationing procedure must be used to limit the eligibility. Location, administrative choice on the basis of additional criteria such as first come first served, sheer chance, and willingness to fulfill the qualification procedure are all criteria which may provide a basis for choice among individuals in similar circumstances.

On a normative basis, questions of horizontal equity are a relevant concern with respect to judging the performance of different policies. Two policies of equal expense may redistribute benefits of similar value solely to the designated group of beneficiaries. Yet, one may redistribute $1,000,000 to a target group of ten thousand eligible recipients by offering a benefit of $100 each whereas, another may offer the same benefit to the same group through a $10,000 benefit to one hundred individuals. If matters of horizontal equity were not of concern, these two policies would be equivalent because each directs $1,000,000 in resources to the target group. A concern with horizonal equity suggests the two policies cannot be considered equivalent.

Much evidence in the form of our legal and institutional arrangements suggest that horizontal equity is an important normative goal in shaping public policy. For this reason, questions of horizontal equity will be one of the criteria used in the assessment of alternative housing policies.

4.2 Vertical Equity

Vertical equity refers to the principle that unequals should be treated differently. The principle of vertical equity stated in this form can be regarded as a direct corollary of the principle of horizontal equity. Whereas horizontal equity was complicated by the need for principles of determining who is considered equal, vertical equity requires both a ranking of individuals and some principle for establishing the appropriate treatment of each rank.

The concept of vertical equity has its origins from the theory of taxation. Like the benefits from government programs, the costs of taxation should be distributed so as to maintain vertical equity. In answer to the question, "To what extent should discrimination in tax rates among separate classes and groups of the population be accepted?" Buchanan declares:

> One thing requires stating at the onset. There are no agreed-on or even widely accepted answers to these questions. Different experts disagree, even if this is recognized as a field where expert opinion is better than any other, a highly questionable recognition in itself. Nevertheless some decisions must be, and have been, made in distributing taxes among separate groups. These decisions have not been made on the basis of purely expedient considerations. Some "principles" have been used, at least in the discussion of alternative tax programs. (p. 102)

4.3 Income as a Measure of Equity

The most frequently used measure for estimating redistributive effects of any policy is its impact on the distribution of current income. Current income, however, is only one, possibly an unrepresentative, observation from a pattern of income over a life cycle. The implications of the life-cycle of income for assessing horizontal and vertical equity must be explored further in order to determine any limitations to the use of current income.

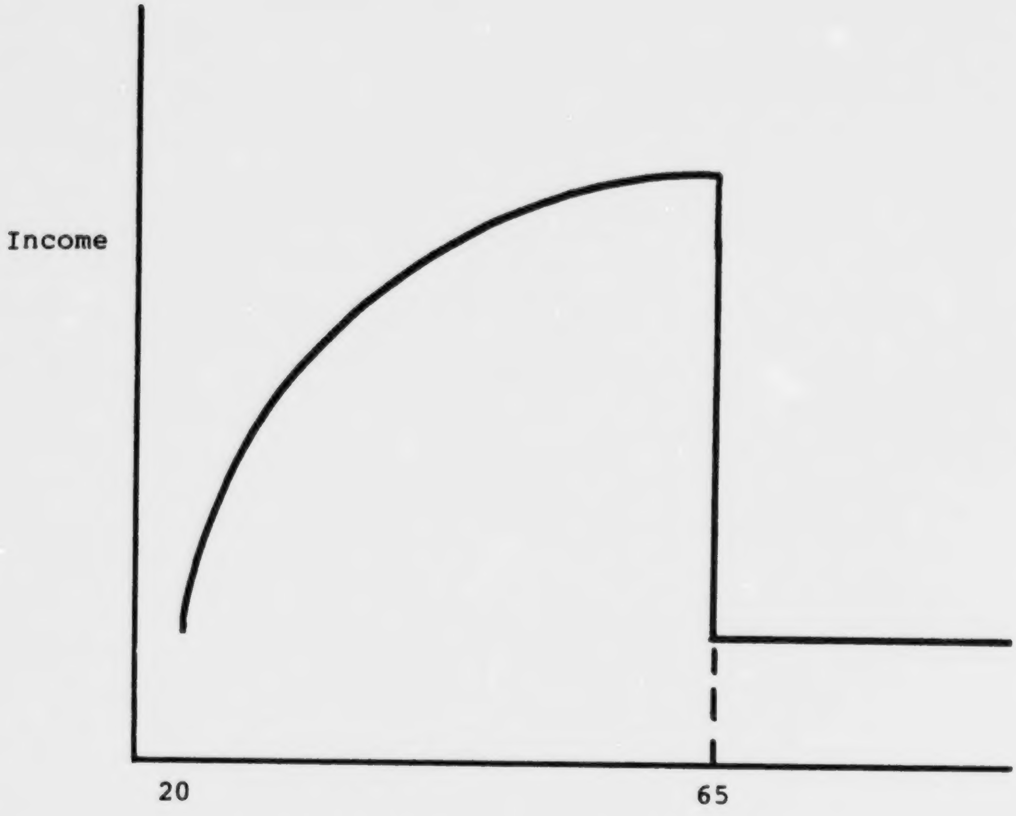
Research on income distribution has shown that income and other economic variables of an individual or household follow a pattern over the life-cycle.(2) Generally, income is low at the beginning of the life-cycle when the individual first becomes independent of the family or forms a new household. The low income reflects the individual's inexperience and relative lack of job market skills. Moreover, individuals entering the labour market generally face a greater probability of unemployment than more experienced workers.

Individuals experience rising incomes with age as they become more experienced. After a point, depending on occupation, individuals' incomes tend to decline before the individual reaches retirement. The decline occurs earliest for manual workers and latest for managers and professionals. Finally, earned income ceases completely at the time of retirement while income from investment continues and any pension income helps to replace earned income. The typical pattern of income over a life-time can be represented by the inverted "U" shaped curve shown in Figure 3.1.

The life-cycle pattern of household income complicates the analysis of the income distribution effects of housing policy or, for that matter, any type of government policy. Current income is, at best, an imperfect measure of life-cycle income. The use of current income as either a criterion for eligibility for social programs or as a measure

Figure 3.1

Life cycle income



Age of individual or household

of the effects of these policies on income distribution must be made with an awareness of the following problems:

i) households differ in terms of the variability of their income around their life-cycle patterns,
ii) at any time, households will be at different stages of their life-cycles,
iii) the life-cycle pattern of income differ among households.

The implications of these problems for present purposes will now be discussed.

i) Variability of Income. Household income does not follow the life-cycle predictably from year to year. Moreover, the degree to which income follows the life-cycle differs among individuals and households. Workers in resource industries, for example, may suffer fluctuations in income resulting from lay-offs in depressed periods on the one hand and gain opportunities for overtime in periods of prosperity. Other occupations such as school teachers or clerical workers may experience more stable incomes because they are less subject to lay-offs.

A major problem arises with programs that incorporate a one-time criterion for eligibility. If incomes were stable, initial qualification according to the intended criteria would ensure that the benefits continue to accrue to the target group as intended. To the extent that incomes are variable, the relative position of various individuals or households will change over time. As a result, incidence of the benefits, while still identified with the same individuals, will no longer correspond with the intended incidence of benefits.

ii) Different Stages of Life-cycle. Two individuals may have different incomes at any time even though they will follow identical patterns of life-time income. This difference arises because individuals of different ages will not be at the same stage of their life-cycle. Consider, for example, a starting school teacher and a school teacher with twenty years of experience. The income of the older teacher may be as much as one and one-half times the income of the beginner. Comparisons of current income might suggest that the disparity of income requires some redistribution. Still, such redistribution might be revised later when the younger teacher is at the peak of earning power and the older teacher has retired. This example raises a fundamental question for social policy. Should redistribution be directed toward individuals and households on the basis of current income or their longer term prospects? The approach taken toward social policy clearly depends on the answer given to this question.

iii) Different Life-cycle Patterns. The pattern of life-cycle income varies from individual to individual, largely dependent upon their occupation. For example, doctors undergo many years of training at low income, following years of high income. Taxi drivers, in contrast, earn a steadier annual income. These differences in life-time patterns can make comparisons based on one year misleading, even though the individuals compared may be the same age. For example, a twenty-two year old taxi driver may earn more than a medical student of the same age. Use of current year income to determine social policy may lead to results that no one really intends. Should income be redistributed from the taxi driver to the medical student?

The last two problems - different stages of the life-cycle and different life-cycle patterns - are very pertinent for housing policy. How should the target groups for housing policy be defined? Should housing policy be directed at households and individuals whose current incomes are low but who almost certainly will experience higher than average incomes through the rest of their lives? This concern is especially relevant for student housing programs of the 1960's. One source of disfavour for these programs may have been a realization that some young low-income individuals and households may be experiencing a low income phase of a pattern in which they can experience an above-average life-time income.

It may be argued that the introduction of the distinction between current income and life-time income only obscures the problem of equity in redistribution and that redistribution should proceed on the basis of current income. Such an argument would make sense if redistributions were costless. Income could be distributed toward groups expected to have high life-time income in their early years and then taxed back in their higher income years. Such a process is likely to be costly in reality. If the resources available for redistribution are limited at any time, the income redistributions toward these groups may come at the expense of others with lower life-time incomes. In addition, the process of taxing back will impose costs because of the distortionary effects of taxation.

The problems posed for policy design by the life-cycle of income cannot be resolved by analysis alone. The questions raised are normative questions that are rarely addressed directly. It is not enough for policy makers to seek to change the distribution of income among individuals or households. The intended equity effects of any policy should be specified in terms of the intended concept of income.

Determination of the redistributive effects of social policies over a longer period than one year requires extensive data which is generally unavailable. As a consequence, most of the redistributive effects of housing policy, cited in this study, are expressed in current income. Thus, we cannot distinguish the source of low income between temporary or longer run factors. Moreover, these measures may not correspond with the redistributive objectives of the policy makers.

4.4 The Interpretation of Equity Effects

As implied by the name, redistributive policies are directed toward changing the distribution of income among individuals. This distribution can be described in terms of the ratio of the income of one individual or group of individuals to the income of another. The distribution of income is expressed in terms of ratios or proportions to make comparisons possible between places or over time. Little meaning is conveyed from the statement that A's income exceeds B's by $500 unless the level of income is known. The $500 difference could be one per cent or one hundred percent. In contrast, the statement that A's income exceeds B's by fifty percent conveys some meaning of the difference. A can purchase twice as many goods and services as B can.

The analysis adopts the three-fold classification used for taxes according to whether their impact is proportional, less than proportional or more than proportional to income. A proportional tax can be considered as a bench mark in that it taxes individuals the same proportion of their income at all income levels. A program yielding benefits can be classified in the same way. A benefit program is classed as proportional if it supplies benefits to individuals in proportion to their income.

To appreciate why proportional taxes and benefits are used as a benchmark, it is useful to consider an alternative which focussed, instead, on the absolute tax burden or benefits. By that measure, a tax which took $100 from a household with $1000 income and $101 from another household with $2000 income might be judged as redistributing income to lower income households. Even though such a tax takes more from the household with higher income, it makes the after-tax distribution less equal than the before-tax distribution. Before taxes, the low income household has half the income of the high-income household. After taxes, the low income household has $900 income whereas the high income household has $1899, or more than twice the income of the other household.

The use of proportions to describe the income distribution leads directly to the use of proportionality as a benchmark for classifying policies. A tax policy or a benefit program which is proportional to income leaves the income distribution as expressed in proportions unchanged. A tax which is more than proportional and taxes a smaller proportion at lower levels of income makes the distribution of income more equal. Similarly, a benefit which is less than proportional and gives a smaller proportional benefit at lower levels of income makes the distribution of income less equal.

The limitations of the proportionality benchmark must be clearly understood. It is simply a measure which answers one question. Does a program of taxes or expenditures make the distribution of income more or less equal after the program than before? It does not answer whether the redistributive effects of any policy are insufficient or too much. These issues require normative judgements.

The proportionality criterion is not the only one which could be applied. For example, policies can be judged according to the absolute benefit going to individuals at different income levels. A policy could be judged by this criterion as contributing to redistribution only if it supplied smaller absolute benefits as income level increases. The absolute difference criterion would be derived from the assumption that the distribution of income is gauged by the absolute differences in income among individuals. As seen above, this measure would be difficult to compare over periods of time in which overall levels of income change. Clearly, it would be a more stringent test of redistribution than the proportionality criterion. Some measures that narrow the proportions among incomes of individuals would not be identified as having redistributed income from higher to lower income groups by this criterion.

Throughout this study, comparisons are generally made on the basis of the proportionality criterion because of the availability of studies using this measure. The measure also has justification from the commonly used measures of income distribution. More important, however, is an understanding of the purpose of the measure. It indicates the effects of any policy on the distribution of income. It does not judge whether these effects were too little or too much.

4.5 Equity Effects of Individual Policies

In some sense it has little meaning to speak of the impact of any single government policy on the distribution of income. While some policies are directed primarily at changing the distribution of income, others affect income distribution only incidentally in the attainment of other objectives. There is doubt about the wisdom of judging a policy on its income distribution effects in isolation. A policy might be justified on the basis of its efficiency in attaining some other goal despite its undesirable equity effects. For example, expenditure on a special learning program for children in one location might enhance the goal of universal literacy, even though it serves only children whose families reside in major metropolitan areas. Extension of the programs to other areas may be prohibitively expensive. By excluding children who reside in smaller centres, the policy is detrimental in terms of horizontal equity. In this instance, policy makers may proceed with this policy even though they recognize that it conflicts with their judgement of horizontal equity. Such a choice may be judged reasonable in light of the fact that the policy is only one among many which affect the households in different ways.

5.0 Adequacy of Housing

The other strand of the affordability objective concerns the adequacy of housing occupied by any household as distinct from the adequacy of income from which their housing expenditure is made. The housing quality objective differs distinctly from the income distribution element of the affordable housing goal. In reviewing the adequacy of housing goal, it is useful to separate three strands of the argument:

1) that it is desirable that recipients gain their benefits in the form of housing;
2) that in-kind transfers of housing provide "external" benefits to other parties; and
3) that housing transfers benefit individuals and households with special needs.

5.1 The Desirability of Housing Benefits

The housing quality goal depends on the proposition that the consumption of housing services differs from the consumption of other goods such as food or clothing in a fundamental way. Moreover, the proposition holds that public policy should be directed towards ensuring that households can receive an adequate level of housing, regardless of their other circumstances. For example, one advocate argues:

> The poorest people among us should live in better housing than they are able to afford and that they should be assisted to do so. (Friedman and Weinberg, 1982, p. 4)

This argument is independent of advocacy for the general improvement of the condition of the poor; the poor should be assisted by policies to gain better housing.

This argument for policies to obtain the goal of better housing for certain groups in society raises several interrelated questions. It may be argued that such policies can be judged as paternalistic to the extent that the poor are helped only to the degree that they are willing to respond by improving the quality of their housing. Accordingly, advocates and policy makers presume to judge that the poor are incapable of judging their own need for more or better quality housing.

A variant of this argument against paternalism is frequently advanced by those who argue that households are likely to be the best judges of their own well-being. Aaron, for example, explains:

> Economists have long held that public provision of commodities below cost to households is less efficient in improving family welfare than unrestricted transfers of income. If the government were to give a family the cash equivalent of its housing subsidy, the family could purchase unsubsidized housing equivalent to that provided by the government. Normally, a family prefers to spend only a part of an unrestricted transfer on any one commodity. From the family's standpoint a cash transfer would leave them at least as well off as would subsidized housing, and usually better off. (1972, p. 9-10)

Similarly, Schelling argues the same point more forcefully:

> A related touchstone of market economics is the idea that most people are better at spending their own money than somebody else is at spending it for them. Sometimes this is directly elevated into an ethical principle: the consumer's right to make his own mistakes. But it is usually simply that giving a poor family a shopping cart filled from the shelves of a supermarket is not as good as giving

> them the money and the cart and letting them do their own shopping. The idea is that they will get more for your money if they go to spend it. A given amount of your money will do more good for the family from the family's point of view if it is spent the way they want it spent. (1984, pp. 25-26)

This criticism, thus, questions the justification for general housing policies in that a family's general welfare can be improved more effectively by general income transfers.

Finally, policies directed to consumption of housing, as distinct from general income transfers, also raise questions from the perspective of horizontal equity. These policies, by their nature, reward households in the target groups which either already satisfy the standards for housing or which are willing to respond to the policy by improving the quality of their housing. In contrast, households who do not meet the housing criterion are excluded from receiving benefits. This argument, in its present form without further elaboration, conflicts with the principle of horizontal equity: equals are not treated equally. Horizontal equity would require the further justification that those who desire greater housing should gain greater benefits than those of comparable income. In other words, households that prefer housing are more deserving than other poor.

A number of responses can be made against these criticisms of the housing quality dimension of the affordable housing goal. With respect to the paternalistic argument, it may be argued that paternalism may be completely defensible, in light of the fact that households may consist of other individuals with different interests than those that actually make the expenditure decisions for the household. In particular, a housing policy may be directed at ensuring that the children of the poor can be assured of gaining the benefits which may accrue from occupying higher quality housing. As Aaron (1981) puts the point graphically:

> My guess is that society would willingly incur high costs to save children from being bitten by rats or to spare them from nibbling lead-based paint. (p. 86)

Still, the limited scope of this argument should be noted: it justifies housing policies directed only toward families with dependent children.

Another variation of this defence for in-kind transfers may be based on the information costs of making consumption choices. Friedman and Weinberg (1982), for example, argued:

> Only if the donor (the public) believes that the families in question will not make the "right" choices (according to the donor's values) should it interfere in this process. The motivation for intervention need not be patronizing, however. A poverty household's "incorrect" choices could result from a lack of information or even misinformation. (p. 130)

As stated, however, the argument leaves open the question of determining which households are well informed and which are not. In addition, it does not consider the apparently simpler remedy of just supplying information to households to help them make better choices.

The economic argument, with respect to the inefficiency of transfers in kind, has been faulted for ignoring the interests of donors. Implicit in these criticisms of transfers in kind is the suggestion that donors are concerned solely with income levels of recipients. Donors may also have an interest in the way in which the income transfers are used. In this case, the transfer in kind serves to achieve the donor's objectives. Even though transfers in kind may not be as beneficial for recipients as would pure income transfers, the overall effect requires a balancing with the donor's interest in the form of the transfer.

A more pragmatic argument suggests that it may be naive to compare direct income transfers with transfers in kind of equal cost. At one level, it is argued that transfers in kind can attract greater political support than general income transfers. As Aaron observes:

> Subsidizing commodities permits political alliances to develop between advocates of assistance to the poor and producers of commodities. (p. 93)

Thus, the choice is not between equal expenditures on the two types of programs, for the redistribution might not be forthcoming if it were restricted to just unrestricted cash transfers. Rather, greater appeal of transfers in kind means that the overall well-being of the poor can be improved to a greater extent by a patchwork of specific transfers than by a program of income support. Moreover, it could be added that while each program may favour various lower income groups on the basis of criteria other than need alone, the overall income distribution effects of such an approach, given the prospect of greater support, may also be more favourable than a policy of general income support.

The same argument in a different guise cautions that, while replacement of in-kind transfers by general programs may be a laudable long-term goal, one consequence of its adoption could be the curtailment of specific programs such as housing without a parallel strengthening of other programs for redistribution. In other words, the choice is between a functioning and imperfect program of in-kind transfers and no more than the prospect of a superior program of general income transfers.

5.2 The Externality Argument

Externalities of consumption form the basis of the second argument in favour of in-kind transfers of housing services. The term "externality" is used by economists to refer to effects of one person's actions on the well-being of others. The most common use of the term refers to pollution and the environment. The wastes from production of wood pulp can ruin the environment for cottagers. As applied to housing, this argument suggests that one household's choice of standard of housing affects the quality of housing which can be achieved by others. In particular, the quality of any household's housing depends critically on the nature of the neighbourhood in which it lives. As Aaron (1972) puts the case:

> Another commodity the occupant of a residence purchases is neighbours. Their behaviour and appearance affect the price prospective occupants are willing to pay for housing... The intelligence, honesty, and other attributes of his neighbours directly affect a homeowner's welfare and influence the value of his housing. For example, academic achievement depends significantly on the socioeconomic status of fellow students... The residents of poor neighbourhoods are victims of high prices, inferior merchandise, high interest rates, and aggressive and deceptive sales practices... Another social cost that varies by neighbourhood is probability of crime. (1972, p. 6)

Thus, measures which assist any household to improve the quality of its housing has a spill-over effect on the well-being of others.

The externality argument supplies a justification for only limited types of housing programs. Housing assistance would be directed to households according to the effects that their current housing has upon others. Assistance would not be determined by the income of the recipient, except to the extent that externalities are judged to be greater from the housing of the poor. The assistance for this purpose would not be offered to households, most typically rural, whose poor quality housing does not have any effect on others. Finally, the assistance would have to incorporate strict requirements which dictate improvement of the characteristics which imposed costs on neighbours and others.

5.3 Special Needs

A final dimension of affordability and housing involves the provision of housing to particular groups with special needs for housing such as the elderly or the handicapped. The Association of Municipalities of Ontario (AMO) explicitly recognizes this dimension, stating:

> The public sector's role should be one where funding is directed to meeting certain service objectives including providing for low and moderate housing needs and for groups with special needs. (1982, p. 10)

This dimension of housing policy recognizes that these groups have housing needs which go beyond the question of affordability. The handicapped may require housing which has been specifically designed to enable them to live as independently as possible. For example, an individual in a wheelchair can live independently better in an apartment when cooking, laundry and other facilities reflect the tenant's use of the wheelchair. Similarly, the elderly may be better served by housing which gives them access to common eating, recreational or health care facilities when they need or desire them.

Although this special needs argument for the supply of housing may be justified on the grounds of paternalism discussed earlier, a justification for the supply of housing for these special groups may be offered which is separate from the other arguments reviewed so far. It may be argued, especially for the handicapped, that their special needs for housing are so individualistic that the costs of relying on the private market would create such large information and transactions costs that handicapped people would bear unreasonable costs in finding suitable housing. In effect, the special needs argument for housing policy can be viewed as an extension of a general form of social insurance by which people are insured, not just for inadequacy of income, but for circumstances which make the costs of everyday living greater.

This explanation remains incomplete to the extent that, in its present form, it appears only to justify greater income transfers than provision of housing in kind. A further step to the argument would have to be that housing programs can overcome these greater costs to special groups more efficiently than the provision of larger income transfers, with the beneficiaries undertaking the search for and acquisition of appropriate housing. In other words, there are economies of scale through performing this function collectively. Whether this argument is correct or not is an empirical matter. Regardless, however, the supply of housing to individuals with special needs appears to be an accepted value of many of those associated with housing policy and, as a consequence, will be among the criteria used to evaluate housing policy from the perspective of affordability and housing.

5.4 What Is Special About Housing?

The reasoning behind the housing quality argument appears generally less straightforward than that behind the adequacy of income argument. Despite all the arguments and counter arguments, the question remains: why should housing be treated differently than other necessities such as food and clothing? Most of the reasons lead to additional problems when pursued further. The argument that donors prefer to give housing and the argument that greater potential support exists for redistribution through housing lack demonstration. How do we know that the presence of many specific transfer programs is not an obstacle to programs of general income support? Might not the public be more willing to improve the adequacy of incomes to a greater degree directly? The externality argument raises different problems of its own. It turns housing policy into "neighbourhood" policy. The tie between low income and housing support becomes tenuous. Housing policy should be directed to alleviating types of housing which impose costs on others. This approach makes it very difficult, for example, to argue for support for rural housing. Nevertheless, the importance of this goal to many means we must consider how to evaluate it.

5.5 The Interpretation of Housing Adequacy

Different standards can be applied for measuring the performance, depending on how the adequacy goal is defined. On the one hand, the housing goal can be defined in terms of the elimination of housing that fails to meet certain criteria of quality as measured by the physical characteristics of the dwelling. By this criterion, the success of a policy is judged by its effects in decreasing the number of households in substandard dwellings. Less important is any increase in the quantity or quality of housing which does not affect the proportion of housing which fails to meet the standard. On the other hand, the success of a housing policy can be judged by some measures of the overall quality and quantity of housing occupied by the target groups of the policy. These measures may be either physical measures or measures of expenditure.

While the judgement of the success of a policy directed toward the adequacy of housing may appear easier, some problems should be noted regarding the evaluation of policies from this perspective:

1) conventional measures of affordability which relate rental payments to income may give a distorted view of the effects of a policy,

2) increased expenditure on housing need not indicate any improvement in quality of housing,

3) the total effects of a program on the stock of housing may differ from the number of units produced under the program.

1) Measures of Affordability.

Frequently, the affordability of housing is measured by some ratio of rental expenditures or other housing costs to total household income. It is possible, however, for a housing policy to enable target households to spend more on housing and have more left over for other things, even though the ratio of housing expenditures to income increases. Consider the following example. Prior to participating in a housing program, a household has an income of $5000 per year and spends $1500 per year on housing. Assume that a housing allowance provides the household with $1000 more per year and the household responds by spending $500 more on housing. As a consequence of the housing allowance, the household spends 0.33 of its income (2000 of 6000) compared to the 0.3 of its income that it spent before the program. Nevertheless, the program enabled the household to spend $500 more on housing and have $500 more to spend on other goods after the program. The ratio of housing expenditures to income will increase, indicating at a superficial level a decreased affordability, whenever households choose to spend a greater proportion of additional income than the proportion that they spent out of their original income. This problem can be overcome by avoiding undue attention to such ratios and by directing attention, instead, on expenditures on housing and other goods.

2) The Effects of Housing Expenditures.

Considering only the direct effects, greater expenditure on housing by target groups is only a starting point to the analysis. It must be asked whether the greater expenditure reflects a greater quantity, better quality or just higher rent for essentially the same levels of housing.

3) The Total Effects on the Stock of Housing.

The number of housing units made available under a supply program might be used as an indicator of a program's effects. Yet, such a measure fails to account for the possibility that the housing units would have been built anyway or that the building of the units under the program displaced other housing units that would have been built in the absence of the program. An appropriate measure for determining the impact of a housing program on the stock of affordable housing requires a comparison of the housing stock resulting from the program with what the stock would have been in the absence of the program.

6.0 Incidence of Cost

The discussion of the redistributive effects of policy has focussed so far only on the proximate beneficiaries of the programs. Another factor to keep in mind are the costs incurred to generate the benefits from the program. The analysis of the incidence of the costs of programs parallels that of the benefits. Programs can be judged in terms of the effects of their costs on horizontal and vertical equity.

A basic distinction was made in Chapter 2 between budgetary and non-budgetary policies. Generally, the costs of budgetary policies are quite evident. Government must raise revenues in order to support its expenditures. Less obvious is the fact that granting subsidies through the tax system must also be financed through increased taxation elsewhere. It is too seldom appreciated that non-budgetary policies also have costs. In fact, this similarity has led to the phrase "taxation by regulation" to describe the effects of non-budgetary policy. Like government expenditures, regulation delivers benefits to one group, imposes costs on another group and creates a deadweight loss in terms of economic efficiency. It is difficult to determine, but, it is unlikely that all these effects correspond to any principles of vertical or horizontal equity. The common characteristic of those paying for the benefits is their participation in the regulated activity. In terms of horizontal equity, they may differ with respect to income, wealth, age and any other relevant characteristics. From the standpoint of vertical equity, the burden of the costs may be totally unrelated to ability to pay.

The costs of programs requiring government expenditures will be distributed according to the incidence of the tax system. The desirability of this distribution of costs depends on the degree of equity which is inherent in the tax system. The impact of the introduction of any new program depends on the sum of the distributional effects of the taxes required to finance it.

An awareness that the distributional effects of programs depends on the distribution of both the costs and benefits is important for assessing the same policy when carried out by different levels of government. The program may have drastically different distributional effects because of the different sources of revenue of different governments. Federal and provincial governments both have a wide range of revenue sources, including personal and corporate income taxes and sales taxes. In contrast, municipal governments are greatly dependent on property taxes. The distributional effects of any policy can also be altered if implemented at either the provincial or municipal level by transfers from other levels of government.

The distribution of cost criterion has only been mentioned here but cannot be followed in the remainder of the study. Any budgetary program could be financed in many different ways. The topic has been raised to stress that the distribution effects of any policy depend on both the distribution of both the benefits and the costs of the programs.

7.0 Effectiveness for Cost

The impact of different policies on the adequacy of income or on the adequacy of housing provides one measure of the policy's effectiveness. Yet, this measure is incomplete in the absence of the costs incurred to achieve that result. Effectiveness for cost provides an additional criterion for assessing the way in which a policy influences adequacy of income and adequacy of housing.

The purpose of the effectiveness of cost criterion is to identify factors which prevent a program from realizing its objectives at least cost. The difference in concept between adequacy of income and adequacy of housing objectives means that different questions must be asked from the perspective of each objective.

The basic question from the adequacy of income viewpoint concerns the improvement in the well-being of the target groups resulting from program expenditures. Two questions are particularly relevant:

1) What proportion of the benefits go to the target groups?

2) How much do the target households value the benefit from the program?

The first question of the benefits flowing to the target groups is essentially a matter of spill-overs. A housing program that is designed to ensure most of the benefits go to the target group can be considered more cost efficient than one which has a major portion of the benefits going to other groups.

The second question, the evaluation of the benefits of a program, is more complicated. In many housing programs, the consumption of housing meeting some standard of quality or percentage of income must be satisfied to be eligible for benefits. Alternatively, the housing benefits may be gained directly in kind through a public housing program. The nature of the housing supplied may not correspond to the housing that would have been chosen by the household in making the same expenditure. Thus such housing does not contribute to household well-being on a dollar for dollar basis commensurate with its cost or even its market price. Rather, this housing expenditure must be valued on the basis of the household's evaluation of the housing services.(3) Expenditures on any administrative mechanism required to assure the use of benefits for housing would be a pure waste from this perspective.

An entirely different perspective is required for assessment of the housing adequacy dimension. This issue can also be distilled into these questions:

1) How much of the benefits are spent on housing?

2) To what extent does the additional expenditure lead to additional housing?

The significance of the first question is straightforward. The adequacy of housing goal is concerned solely with the housing occupied by the target households. Failure of target households to spend their allowances on housing reflects an inefficiency of the program, increasing the cost relative to the increased housing services gained.

A more difficult question arises with respect to the interpretation of the housing services produced under the program. To what extent are these housing services net additions? This question can be interpreted in two senses. First, to what extent have the gains of target groups come at the expense of the quality of housing consumed by other groups. In this case, it must be determined whether the housing program affected the rents or availability of housing to other groups of households. Second, to what extent would the housing attributed to the program have been created in its absence? To the extent some of the housing would have been available anyway, the costs of the program - housing costs above the cost of alternatives plus administrative costs - should be attributable only to the net additions to housing created by the program.

8.0 Rent Gouging

Stanbury (1984a) suggests that:

> The most frequent and apparently most powerful argument used by the advocates of some form of rent control in Ontario in 1975 was that controls were necessary to prevent the "gouging" of tenants or to prevent "unconscionable" increases in rents. (p. 2, 3)

Despite the importance of this objective to housing advocates, unfortunately, there is no unanimity as to what it means. Stanbury (1984a) identifies a number of possible meanings:

> Concept 1: Gouging may be defined as setting a monthly rent above the prevailing market rent for comparable units.
>
> Concept 2: This concept of gouging concerns the relationship between rent increases and the landlord's increases in costs and/or rate of return.
>
> Concept 3: This concept of "gouging" is based on the repudiation of widely held expectations.
>
> Concept 4: Gouging may be perceived in the case of rental increases which amount to a form of "catch up".
>
> Concept 5: The perception of "gouging" may be related to the speed of adjustment to economic change.

Concept 1 appears to differ in kind from the other concepts of "gouging" examined by Stanbury. Concept 1 can be viewed as a static "gouging" argument in that it is concerned with comparative levels of rent at any given time. In contrast, each of the other concepts of gouging refer to the change of level of rent relative to some standard: landlords' costs, expectations and speed of change.

In his analysis of the objectives of rent regulation, Stanbury emphasizes Concept 2: the relationship between rent increases and changes in landlords' costs. Though not identical to Concepts 3, 4 and 5, it does appear to capture the same types of concern in that they all may seem related to some concept of fairness.(4) This overt emphasis on change is quite appropriate, given the introduction of controls during the period of increasing inflation during the 1970's.

In a more stable environment, the concerns with respect to housing policy extend beyond changes in rent to the patterns of rent levels. Greater emphasis would thus be placed on any landlord setting rents above prevailing market rates to take advantage of ignorance on the part of tenants or some source of tenant immobility.

The "gouging" issue has been shown to cover both static and dynamic arguments. Both appear to be concerns of housing advocates. As mentioned above, however, the policies reviewed here can be considered as long-term policies which would have only limited impact on short-run or dynamic adjustment problems. Thus, for the purposes of this study, attention is directed toward the static concept of gouging (Concept 1).

The weighting that should be attached to the prevention of rent gouging in the formulation of housing policy is difficult to determine. As already mentioned, the definition of the term itself is unclear in that several different meanings are attached to the phrase. Even if agreement were reached as to the concept, a further question needs to be asked about the prevalence of rent gouging and about the ability of tenants to escape its consequences. Normally market pressures could be expected to limit the possibilities of rent gouging. Nevertheless, certain groups, in particular the elderly, may be poorly informed or may have to bear substantial economic and psychic costs in moving. These groups may be prone to facing what the public would view as unconscionable rents. This possibility should not be confused with reality. Before much emphasis is placed on the prevention of rent gouging as an objective of housing policy, some indication of the dimension of the problem would be desirable. It could indicate both the need for this emphasis and the appropriate approaches to be used to overcome the problem.

9.0 Security Of Tenure

The security of tenure issue embodies direct conflict between the interests of tenants and landlords. Makuch and Weinrib (1985) distinguish the economic and psychological aspects of security of tenure from the tenant's viewpoint. Security of tenure in an economic sense refers to the problem of affordability whereas, security of tenure in a psychological sense is intended "to ensure that the tenant has security of tenure similar to that of a purchaser of a home" (Makuch and Weinrib, 1984, p. 2). Security of tenure conflicts with provisions that:

> Enable landlords to regain their premises for their personal use or for redevelopment, to protect the quiet enjoyment of the premises of other tenants, to deal with damage by tenants beyond regular wear and tear and to prevent tenants from willfully misrepresenting the premises to prospective purchasers. (Makuch and Weinrib, 1984, p. 2)

The security of tenure criterion overlaps to a degree with other criteria proposed for the purposes of this study. Security of tenure in the economic sense can be considered the equivalent of the criterion of affordability of housing developed above and will be treated in that context. The relationship between the psychological aspect of security of tenure and the landlord's prerogatives will be discussed wherever it can be identified that a housing policy impinges upon that relationship.

10.0 Economic Efficiency

The economic efficiency criterion for assessing housing policy refers to any effects the policy may have in directing resources toward or diverting resources away from their highest valued use. Two possible sources of inefficiency which which result from changes in housing policy are examined in this study. The first source consists of any change in information or transactions costs whereas, the second consists of any change in the incentives to use housing and other resources efficiently.

10.1 Information and Transactions Costs

The operation of the market mechanism is not costless for buyers and sellers. In some markets, such as the stock market, market professionals create formal market institutions and charge other participants for their use. Even here, the explicit costs for using the market facilities may be only a fraction of the costs to buyers and sellers from using the market. They must also bear the costs of gaining information about market conditions and the costs of reaching and enforcing transactions with others. In most markets, a formal market mechanism does not exist and the costs to buyers and sellers from using the market are less likely to be explicit but can be measured in terms of their time and effort of the participants themselves.

Informational costs are an important element of the costs of participating in rental housing markets. Both tenants and landlords have an interest in informing themselves of the market opportunities available to them.

They value information because uninformed decisions can lead to costly mistakes. An uninformed tenant faces the risk of being locked into a lease for an unsuitable dwelling or having to bear the cost of an extra move. Similarly, landlords may be forced to suffer excessive vacancies from being uninformed. Still neither landlords nor tenants will seek to become perfectly informed; acceptance of some risk of making a mistake may be cheaper than the acquisition of complete information.

Buyers and sellers also incur costs directly in the process of carrying out transactions in any market. These range from the explicit payments made to gain legal assistance in formulating the terms of a contract through the need to keep records for taxation and other regulatory purposes, to the expense of monitoring the performance of the other party and settling disputes which arise between the transacting parties.

Markets differ substantially with repect to the information and transaction costs which must be borne by buyers and sellers, according to the nature of the commodity transacted and other special considerations. Some markets can operate very simply with little expense to the buyer and seller. Low transaction costs are more likely, the more homogeneous and simple is the commodity, the more clearly there are repeated transactions between any buyer and seller, and the more likely the dealing consists of a spot transaction which does not involve further commitments on the part of either party.

Government policies can influence the costs of using the market in a number of ways. Some government policies are directed toward making it easier for market participants either to gain information or to carry out transactions. Sometimes, these policies may achieve the objectives by coordinating producers so as to supply similar comparative information to purchasers. Still, these policies require the producers to incur additional costs to conform to the government regulations. Whether the benefits of such a policy outweigh the costs cannot be determined without a case by case analysis.

Government policies directed to other purposes can also influence the costs of market transactions as a side effect. The government's monopoly of the control of liquor sales, for example, has the direct effect of raising prices to the consumer. But, it also has several indirect effects. It leads to standardized prices, which presumably reduce the costs of transacting. In contrast, a smaller number of outlets increases the cost to the consumer in terms of the time and effort required to make purchases.

Rental housing has many characteristics which suggest information and transactions costs are likely to be significant. Hulchanski (1984) observes that each dwelling differs with respect to age, size, state of repair, amenities, quality and location. Stanbury (1984a) enumerates the transactions costs of landlords and tenants:

tenants

- outlays for information
- opportunity cost of search time and travel costs
- moving costs
- re-decoration outlays
- psychological and economic costs and disruption and altering patterns of travel, shopping, etc.

landlords

- advertising costs
- rental agency costs
- vacancy costs (revenue lost)
- risk of bad tenants (damage, non-payment of rents, noise)
- cleaning and decoration costs

The significance for present purposes of the information and transactions costs in the rental housing market is not that they are high or low. Rather, their significance arises because they are capable of being influenced by government policies directed toward the housing market. Thus, policies which increase information and transactions costs cause more resources to be diverted to the purpose of transacting and away from other uses which contribute more to the public's well-being.

10.2 Efficiency of Housing Use

A final aspect of economic efficiency is the efficiency with which the housing stock is used. Crucial to this issue is the question of consumer choice. Does the housing program permit households to make whatever choice of housing that best satisfies their needs and is consistent with their resources?

The question of choice is important in a number of ways. Choice for consumers can be viewed as an inherent virtue in itself. Those things chosen by consumers on their own are likely to be valued more highly than an arbitrary selection made by others. The choices by individuals reflect their preferences in face of a spending constraint whereas, an allocation by others can reflect, at best, their judgement of the preferences.

Choice is also important from the standpoint of the efficiency of housing use. Different households do not value all dimensions of housing equally. Does the amount and quality of housing fit the household's needs, or must the household suffer with respect to the inappropriateness of some dimension of households to meet its need on other dimensions? Does the program give a choice to the household between size and quality? Does the household have a choice of location or is it constrained to choice among just a few locations.

The matter of choice becomes more important over time. A program may permit a household, initially, to obtain housing that fits its needs. But over time, as a household's housing needs change as the household ages, grows or shrinks in size, experiences different levels of income or as its desired locale changes as its employment opportunities change, the scope for flexibility becomes important. What sorts of incentives does the program offer to households to change the nature of its housing within the program without excessive cost. The significance of this issue extends beyond the household in question. A household which is constrained to occupy housing that is unsuitable to its needs may be preventing other households whose needs correspond to this housing from occupying it.

10.3 General Economic Efficiency

A final and important dimension of economic efficiency arises with respect to the role of relative prices in allocating resources to their highest valued uses. In the absence of distortions, prices reflect the value of resources in their alternative uses. The willingness of any user to pay the prevailing price reflects the user's valuation of the resource that at least equals the valuations placed by others on the resource. This conclusion applies to all economic resources: the services of housing or productive inputs such as labour and capital.

Any housing policy necessarily alters relative prices and the allocation of resources. The manner in which they do it differs from policy to policy. Rent regulation affects prices directly by setting limits on allowable rents. Other policies alter prices by changing supply directly or by encouraging or assisting private demanders and suppliers. The way or degree to which prices are affected by housing policy determines the degree to which economic efficiency is affected by housing policy.

11.0 Diversity and Balance in Communities

Another factor that needs to be taken into account in this study arises in a number of different forms in discussions of housing policy. Generally, this criterion can be referred to as "diversity and balance in communities." More specific meanings of the criterion depend on the scope of the relevant community.

This criterion, as will be seen in Chapter 6, played a major role of the critique of public housing, which occurred in the early 1970's. Public housing had the disadvantage that it lacked the diversity found in other neighbourhoods. From this viewpoint, public housing was criticized as creating ghettos of low income housing.

More recently, a different meaning has been identified with the general goal of diversity. As Stanbury (1984b) notes, the Planning and Development Department of the City of Toronto states:

> The City's chief housing objective is to maintain the diversity of its social fabric. (1982, p. 27)

This statement, in apparently placing diversity above adequacy of income and adquacy of housing, shows how seriously this concern is held.

In many ways, these two dimensions of diversity appear similar. Stanbury (1984b) points out that the Central Area Plan of 1976 includes among its objectives:

> A mix of
>
> - households by size and type (families with children, singles, etc.)
> - households by size of income (low and moderate incomes as well as the affluent). (p. 1)

Each of these appears to be wholly consistent with the earlier concept of diversity.

The scope permitted for household choice should be an important determinant of the ability to gain diversity. The ability of recipients to make choices permits an opportunity for diversity within and among neighbourhoods. Housing programs vary with respect to the degree of choice offered to recipients relative to other renters. When recipients have the same choices as others, some may choose ethnic neighbourhoods, some may choose integrated neighbourhoods. A diverse variety within and among neighbourhoods is likely to develop when all renters, whether recipients or not, are given the fullest range of choice to use their available resources.

12.0 Administrative Efficiency

Administrative efficiency refers to the costs involved in running the government mechanism required to administer a government program. These costs are the counterpart in the government sector of the transactions costs of operating a market which were discussed under economic efficiency. They include both the direct costs to the government itself in establishing a bureaucracy to administer the rules and procedures of the program and the indirect costs which must be borne by the public in responding to the program.

The central question with respect to the direct costs concerns the administrative apparatus. What sorts of administrative mechanisms are required to operate the program? Must eligibility and level of support be determined on a case by case basis? Must there be a rationing mechanism? Must decisions be made about the characteristics and location of housing? Is government involved in the planning, construction and maintenance of rental housing? Must housing standards be verified? Are adjudication procedures necessary for resolving disputes? Taking these considerations into account, Trebilcock *et al*. (1982) conjecture:

> That the relative administrative costs of the principle forms of expenditure might roughly be ranked in ascending order as follows:
>
> - demogrants (e.g., OAS, Family Allowances);
> - income-tested transfer payments to individuals (e.g., GIS);
> - compulsory pension plans (e.g., CPP);
> - tax expenditures for individuals and businesses;
> - subsidies to businesses, including subsidized loans;
> - compulsory insurance programs (e.g, UIC);
> - highly discretionary grants to business (e.g., the R & D grants of ITC, and the "new job creation" grants by DREE);

> - highly conditional welfare payments to individuals and families (e.g., CAP); and
> - provisions of public services (e.g., defence. hospitals, schools and roads). (p. 62)

A corresponding list could be developed for housing. Unconstrained housing allowances would be at the top whereas, public housing would probably be at the bottom.

Nevertheless, Trebilcock et al. (1982) suggest that:

> The administrative costs are such a small proportion of the total expenditures that, like taxes, it is difficult to imagine a decision to adopt a particular form of expenditure being influenced by administrative cost minimization considerations. (p. 61)

While this argument may be correct as far as it goes, Trebilcock et al. go on to say that administrative costs within government are paralleled by costs borne by market participants in complying with the government program. Costs of compliance can easily outweigh the administrative costs to government. These costs are likely to rise pari passu with the administrative costs within the government (Trebilcock et al., 1982, p. 62). Trebilock et al. survey the range of requirements:

> Filling in one form and supplying a copy of a birth certificate is all that is required for OAS payment entitlements. On the other hand, applicants for industrial grants usually have to spend much time, energy and money in supplying the required information and in assembling a persuasive written argument. Obviously mothers' allowances, for example, are probably even more onerous relative to the amounts obtained: frequent interviews, inspections, forms and so on. Hosts of professional and not so professional social service workers and administrators are involved in "helping" the putative beneficiaries. (p. 62)

Despite their discussion of the costs of compliance and its association with administrative costs, Trebilcock *et al*. argue that "it seems most unlikely that the minimization of these costs have had much bearing on the choice of forms of expenditure" (p. 63).

A further dimension of administrative efficiency beyond those considered by Trebilcock *et al*. that should be explored is the flexibility of the housing program to changing conditions. To what extent can adjustments be made to changing needs for policy within the framework of an existing program? How costly are modifications to a program if adjustments cannot be accommodated within its current format? The costs discussed here go beyond the explicit administrative costs of the program, to the costs incurred with respect to the goals of housing policy resulting from the persistence of inappropriate policies.

The disturbances to which any housing policy must adapt can be grouped into real and nominal disturbances. Real disturbances are those that change the demand for housing accommodation and can result from demographic change such as the formation of new households or immigration from other regions or countries or from increased expenditures on housing resulting from generally higher incomes. Nominal disturbances usually reflect generally higher prices which raise rents along with other prices but do not represent any increased real demand for rental housing.

The responses to each of these types of disturbances should be entirely different. The real disturbance causes a change in the real demand for housing. While the end result may consist of both greater housing consumption and higher rents, a housing program should permit a response by which the quantity of housing can increase in those areas where the increased demand has occurred. In contrast, while the nominal disturbance changes the affordability of housing, by itself, it need not always require a greater quantity of housing. Rather, the problem becomes one of assuring the continuing affordability of existing housing to the target groups.

13.0 Feasibility

A final factor which must be taken into account is the fact that many policy proposals which have the utopian appeal of satisfying the criteria discussed above still do not become implemented because they fail to take into account the practical considerations of the real world. The feasibility criterion examines the important step of moving from theory to practice.(5) In doing so, it considers some of the major problems likely to be encountered in the implementation of any program.

13.1 Level of Government

Public policy in Canada must take into account the roles of different levels of governments and the need for coordination among them, factors which would not be relevant to policy design in a unitary state. The design of policy should reflect the choice of that level of government which is most appropriate for the policy in question and also the design of mechanisms which keep the costs of coordination among governments at a minimum.

For some tasks, local governments may be more suitable than either the federal or provincial governments. Local governments appear to have one important advantage relative to higher levels of government. They are in a position to have a more intimate knowledge of local needs and problems. A local government which has planned a housing program of its own would be more willing to alter zoning or other building requirements where appropriate and give speedy approval for its own program than for an identical program put forward by another level of government. Such an action need not be a reflection of any bias; there may be inherent economies in planning and approving any project at the same level of government.

Policy proposals also differ with respect to the degree of cooperation required between levels of government. Different levels of government have been assigned different powers by law. If the appropriate powers are not within the scope of the government desiring the change in policy, it must either negotiate with the other government to undertake the program itself or alternatively, proceed with the policy at the risk of confrontation with the other government. This latter alternative may be blocked if it is found to be beyond the limits of provincial powers.

The questions of appropriate level of government and the need for cooperation among governments has special relevance for this study. The Commission of Inquiry into Residential Tenancies is a provincially created body. In making its recommendations, the Commission must be fully aware of the political environment in which it operates. How much scope does the provincial government have to make different changes? Are the best policies in other dimensions outside its powers? The Commission must also consider the need for cooperation with other levels of government, in order to achieve its goals. The considerations may change substantially in the near future. The Globe and Mail (July 15, 1985) reports:

> The federal Government apparently is poised to transfer the bulk of its social housing programs to provincial control... Each province and territory is to negotiate its own housing agreement with the federal agency, Canada Mortgage and Housing Corporation, changing the approach from one national policy and set of programs to a patchwork system varying from province to province.

13.2 Problems of Different Communities

Policy choices are frequently discussed in the context of stereotype constituencies. Such stereotypes may reflect accurately the dimensions of a typical or the most numerous types of community. In reality, a policy should be designed to accommodate the needs of a wide range of communities. Housing policy for Ontario must be adaptable both to the needs of urban Toronto and the smallest communities of the far north. It must be able to reflect wide differences in rental market conditions. For example, in April 1980, the vacancy rate for apartment structures of six units and over ranged from 1.0 per cent in Thunder Bay to 5.3 per cent in London (Stanbury and Vertinsky, 1985). Realistically, any policy is unlikely to meet these needs simultaneously and some choice may have to be made across the interests. Some approaches to housing policy may be readily adaptable to the needs of different communities. In some cases, however, the superiority of an approach for one setting may dictate its use even though it contributes little in other settings. An appropriate solution to a provincial housing problem may not be a single policy directed to both objectives. Such an approach may incur the costs of failing to meet either objective well. The use of several policies may permit more precise targeting of each objective.

13.3 Political Considerations

Many economic policies, shown to be efficient in an economic sense, have failed to be adopted by governments in power and vice versa. As Trebilcock et al. (1982) convincingly argue, the implementation of policies does not depend on the impeccability of social or economic arguments in their favour but rather on their possession of sufficient appeal to self-interested parties to create a sufficiently large coalition to gain political support. They disparage especially:

> The notion that governments can be looked upon as ignorant, benevolent dictators who want to do the "right" thing, who are all powerful, and who are simply waiting for economists to tell him, her, or it what to do. (p. 104)

Despite this harsh realism with respect to the formulation of policy, Trebilcock et al. do see some role for analysis as an input to public policy:

> Although the views of economists and social scientists on normative matters have no particular merit, disentangling the full and longer-term implications of alternative policies can presumably improve policy when politicians have options consistent with their political survival....(W)e are inclined to believe that when politicians perceive that they have such choices they are likely to choose, on the basis of the information available to them, policies that affect broadly

> based longer-term interests rather than policies that pander to narrow short run interests. Economists, and others, can assist them to make choices by providing them with more or better information on the policy implementations of the options. (p. 104)

The policy process, however, extends beyond the response of the politicians to the responses of voters. Trebilcock *et al*. argue:

> Casting a ballot is a policy decision for the voter, as is the decision to join a pressure group... Economic research, by providing a public good, can add to the information available and improve these private decisions...if it is disseminated. It is important to recognize that by influencing voter knowledge and understanding, and hence voter decisions, the insights of economic research (and social science research generally) can be brought to bear on the ultimate decision-making process.... Politicians cannot, however, ignore voters armed with relevant research. (p. 104)

Thus, a practical matter to be considered in any analysis of a policy must be how information of its effects will impinge on the interest of various constituencies of the public.

The interest groups directly concerned with rental policies are quite easily identified. Obviously tenants, landlords and developers all have a substantial stake in central policy. Tenants desire low rents for high quality housing; landlords are interested in favourable rates of return on their investments, and developers want a strong demand for new rental housing. Less obvious are the interests of taxpayers at large. They wish that the goals of housing policy be achieved in terms of the lowest tax burden possible. The interests of any voter may reflect a combination of roles; tenants, landlords and developers are all taxpayers.

The political feasibility of any policy cannot be judged in isolation. The ranking of different policies in terms of their political attractiveness will depend on the current state of housing policy. For the purposes of the present study of examining complementary policies to rent regulation, the most appropriate benchmark is the status of the different interests under the present system of rent regulation.

14.0 Conclusions

Rental housing policy has become the concern of a wide variety of interests including tenants, landlords, developers and builders, bureaucrats, politicians aspiring to be elected, and not least, citizens generally in their role as taxpayers. The interest and concerns with respect to rental housing policies which motivate these groups cannot be expected to be the same. Different groups will make different choices in face of the same trade-offs among objectives. Moreover, what is a trade-off for one group may not be a trade-off for another group. Only one of the objectives which poses the trade-off dilemma for one group may be of interest to the other group.

This diversity of viewpoint makes it impossible to formulate a single set of evaluation criteria which could provide a single uneguivocal ranking of housing policies with respect to their desirability. The purpose of this chapter has been directed toward enumerating the different criteria which interested groups would apply to the evaluation of rental housing policies. Table 3.1 shows the evaluation criteria which have been identified together with key questions based on their criteria. These questions supply the basis for the evaluation of alternative housing policies which follows in the remainder of this study.

This chapter has examined the evaluation criteria to be applied to the evaluation of alternative housing policies. These evaluation criteria, together with the classification system developed in Chapter 2, provide the framework which will be used in the following chapters to assess alternative housing policies. Demand augmenting policies, as represented by housing allowances, are assessed in Chapter 4. Supply augmenting policies are discussed in Chapter 5 and market replacing policies in Chapter 6.

TABLE 3.1

Summary of Criteria

Criterion	Key Questions
A. Affordable Housing	
Affordability and income	- target group for benefits - determinants of benefits - eligibility - participation - size of benefits
Affordability and housing	- proportion of benefits directed to housing - effects on housing quality - effects on quantity of housing - housing for special needs
Incidence of cost	- method used to finance benefits - incidence of costs
B. Effectiveness for cost	
a) affordability and income	- benefits beyond target group - other excess costs to deliver benefits
b) affordability and housing	- additional housing beyond target group - benefits to landlords of existing housing
C. Prevention of Rent Gouging	- reduction of above market rents - eased impact of above market rents on tenants
D. Security Tenure	- effects on tenant's security
E. Economic Efficiency	- effects on information costs - effects on transactions costs - effects on recipient choice - effects on housing use - degree of flexibility
F. Diversity and Balance of Communities	- degree of mix

TABLE 3.1 (cont'd)

G. Administrative Efficiency	- direct costs of administrative apparatus - indirect costs to public from administrative apparatus - flexibility of policy to changing needs
H. Feasibility	- appropriate level of government for implementation - need for cooperation among governments - adaptability to community needs - basis for political support

Notes to Chapter 3

(1) Marks (1984) p. 5. The quote itself is cited from Dennis and Fish (1972), p. 2.

(2) The life cycle hypothesis was first developed to explain household consumption behaviour by Franco Modigliani and his associates. See Modigliani and Brumberg (1954) and Ando and Modigliani (1964). Subsequently, life-cycle analyses have been fruitfully applied to many aspects of individual and household behaviour. See, for example, Fuchs (1983) and Easterlin (1978).

(3) The adjustment reflects the income and price elasticity of demand. See, for example, Aaron and von Furstenberg (1971).

(4) See Knetsch et al. (1984) for a discussion of perceptions of fairness.

(5) The word "feasible" is often misused. The present usage corresponds to Webster's "capable of being managed, utilized or dealt with successfully."

CHAPTER 4: ASSESSMENT OF DEMAND POLICIES

1.0 Introduction

Chapter 3 developed a framework to assess alternative housing policies. The next three chapters apply this framework to assess demand policies, supply policies and market replacing policies, reflecting the classification scheme developed in Chapter 2. Since each of these broad types of policies encompasses many distinct programs in practice, and endless number in theory, the analysis which follows is based on stereotypes of each type of policy. Wherever possible, judgements are made on the basis of the evidence accumulated from actual housing policies in Canada which are examples of the relevant type of policy.

This chapter considers the workings and the consequences of demand augmenting policies. It will be recalled from Chapter 2 that demand augmenting policies are those that work through influencing tenants' costs and opportunities, given any set of market prices. Many policies, actual and proposed, appear to fit this definition: housing vouchers, shelter allowances, rent supplements, housing allowances, rental rebates and housing income supplements. Since housing allowances are the most intensively studied form of these policies, they will be used in this study as being representative of demand policies, in general.

The analysis in this chapter proceeds by steps. Section 2.0 discusses the distinctions among constrained and unconstrained housing allowances with some attention directed towards the types of constraints which have been proposed or used. Unlike some other types of housing programs, the major evidence with respect to housing allowances comes from a unique and extensive experiment with housing allowances which was performed in the United States. Section 3.0 describes this experiment and the types of evidence derived from it.

Much of the difference between constrained and unconstrained allowances arises with respect to two criteria: adequacy of income and adequacy of housing. An unconstrained housing allowance is examined with respect to its working and in relation to these two criteria in Section 4.0. This analysis also serves as a benchmark for examining the effects of the introduction of constraints. Section 5.0 presents the analysis of two types of constraint: i) a rent constraint which bases assistance on actual rent paid and ii) an eligibility constraint which establishes preconditions for receipt of assistance.

Housing allowances have been criticized by some because they expect that any beneficial effects will be dissipated through upward pressure on market rents. The evidence with respect to this criticism is reviewed in Section 6.0. Sections 7.0 to 11.0 review housing allowances in general, with respect to the other evaluation criteria developed in Chapter 3.

2.0 Housing Allowance Allocations

Streich and McClain (1978), in their background paper on housing allowances for the Canadian Council on Social Development, identify commonly accepted components of housing allowances:

> - a direct, cash transfer is made to a family or individual
> - the recipient is given a series of regular (usually monthly) payments
> - the allowance is made to households unable to afford adequate housing
> - the recipients select their own houses or apartments
> - the allowance is portable when the recipient moves to another unit
> - the allowance relies on the use of the existing housing stock
> - the allowance is generally related to "need" based on income, family size and shelter costs, although some ceiling or maximum dollar amount is usually specified
> - the allowance is conditional, that is, it must be used to pay rent or home-ownership costs
> - a housing allowance may be tied to a specific standard of housing. (p. 6)

These considerations lead Streich and McClain (1978) to define a housing allowance as:

> A direct cash transfer made regularly to families or individuals to enable them to afford adequate housing of their own choice from existing units; the amount of the allowance is based on income and housing costs, and is used solely for meeting their costs in their present unit or in another unit if they move. (p. 6)

A notable part of this definition is that the housing allowance must be specifically directed to housing expenditures. Walker (1975) objects to this approach because:

> These formulae do not protect people from the hardship caused by what they _must_ spend on shelter but from the seeming hardship that occurs because of what they _do_ spend. (p. 207)

As an alternative, Walker (1975) proposes a less restricted version of a housing allowance:

> 1. The amount of income supplement is tied directly to the cost of basic accommodation for each type of recipient...
> 2. The formula provides a supplement that is determined by the cost of basic shelter in the area where the recipient lives, and would

> provide in itself no incentive to the recipient to move from one region to another.
> 3. The formula provides a flexibility in the target shelter cost-to-income ratio that is reflected in the income supplement itself.
> 4. There is an automatic change in the income supplement to reflect changing circumstances... since the supplement is tied to the cost of basic accommodation. (p. 207)

The conflicting views on housing allowances appear to extend to all forms of demand policies. The comparison of the Streich and McClain and Walker definitions of housing allowances illustrates that differences may occur in seemingly similar concepts of demand policies. To deal with these differences in a comprehensive manner would require an encyclopaedic analysis of not only all the demand policies, but also all of their variants. Such an approach would inevitably lead to an obstruction of the forest by the trees, if not the branches and leaves.

The strategy pursued in the present analysis of the design of housing allowances is to examine only the two dimensions of demand policies which are important for the assessment of them as alternatives for achieving the possible goals of rent regulation discussed in Stanbury (1984a). That approach is consistent with the objectives of the study.

One fundamental dimension of demand policies is the degree to which households are permitted to make their own housing choices. Many forms of demand policies do not constrain the housing choice of households receiving assistance.(1) More stringent forms require the housing occupied by beneficiaries to meet specified minimum standards, or even require beneficiaries to occupy specified housing units.(2) Housing allowances, or other demand policies which require minimum physical standards do not appear to have advocates in Canada. However, this approach was used by the demand experiments in the United States.

The second fundamental dimension of demand policies is illustrated by comparing the views of Streich and McClain and Walker, noted above. Their differences stem from the standard which is used in determining the subsidy provided. Streich and McClain prefer that actual housing costs, up to some limit, determine a household's benefit. This form of subsidy, which is intended to require that the housing allowance is spent on housing, has also been proposed by Dennis and Fish (1972), Steele (1984) and endorsed by the Canadian Home Builders' Association and the Ontario Economic Council. Their proposals limit the subsidy paid to the actual rent payments of households, using a rent-to-income ratio criteria.

Walker, in contrast, argues that housing costs in general, not an individual household's expenditure on rent, should determine the size of the benefits. Households should have the freedom to spend the benefit as they see fit without being penalized if they do not spend it on housing.

This difference in emphasis in program design appears to result from the different emphasis that the authors place on different goals. Streich and McClain place a higher value on the adequacy of housing concern whereas Walker emphasizes the adequacy of income concern. In effect, Walker's (1975) proposal is a form of general income assistance related to local housing costs.

3.0 The Experimental Housing Allowance Program

Much evidence, with respect to market augmenting policies which work through the demand for housing, has been accumulated through the Experimental Housing Allowance Program (EHAP), established for the purpose of determining the effects of a housing allowance-based housing assistance strategy by the U.S. Department of Housing and Urban Development in 1970. These experiments, when complete, will have cost $160 million, with $80 million going in payments to families and $80 million going for data collection and research (Aaron, 1981, p. 96). Since the results of this program are an important source of evidence for the effects of demand side policies, it is useful to outline and assess the design of these experiments before proceeding to discuss the results.

Three separate experiments were undertaken under EHAP. The two experiments undertaken under EHAP which were most useful for present purposes are the demand experiment and the supply experiment. These experiments were designed to explore:

> (1) How do families respond to housing allowances?
> (2) How are housing markets affected by allowances?
> (Allen, Fitts and Glatt, 1981, p. 3)

A separate experiment was directed to each of these basic questions. Despite the titles of demand experiment and supply experiment, each experiment was built around roughly similar programs of housing allowances made to households. Nevertheless, substantial differences in experimental design mean that the results of each experiment provides different types of information with respect to the workings of housing allowance programs.

3.1 The Demand Experiment(3)

The demand experiment was directed primarily at the ways in which families respond to housing allowances. Allen *et al.* (1981) outline the specific questions to which it was addressed:

> - Who participates and how are participation rates affected by program features such as payment levels?
> - Does a housing allowance program cause participants to move to new locations?
> - What portion of the allowance payment is used for housing?
> - Does the quality of housing improve for participating households?
> - What are the major differences in household responses between a payment program constrained by housing requirements and a program not so constrained, such as welfare payments.
> - How do housing allowances compare with other housing programs in terms of participation, housing quality attained, locational choices, and costs? (p. 4)

The demand experiments consisted of a program of a variety of different types of housing allowances to a selected group of 2,500 households in the two metropolitan areas of Pittsburg, Pennsylvania and Phoenix, Arizona. These sites were chosen on the basis of a number of criteria. With populations in excess of 500,000 and vacancies in excess of 6 per cent, they each provided an environment where housing allowances would be unlikely to exert significant upward pressure on rent levels. The two sites also differed in dimensions of interest to policy makers:

> Pittsburg is a slowly growing, older city with a large black population; Phoenix is a rapidly

> growing, newer city with a large Hispanic population. (Allen *et al.*, p. 5)

Those differences in the sites were designed to indicate whether the particular nature of the markets in which the program was conducted influenced the results in any significant way.

The demand studies incorporated features which permitted a comparison of the behaviour of the recipients of housing allowances with other households. Approximately 950 control families were also identified and data on their subsequent behaviour was collected on the same basis as the recipient families. In addition, detailed information with respect to income, current housing conditions, expenditures and preferences and housing demographics were obtained from some 4000 households before final selections of the recipient households were made.

A variety of different forms of housing allowances were administered to the target groups. The experiment distinguished between unconstrained and constrained housing allowances. Unconstrained housing allowances provided households with transfer payments without any regard for the nature of the housing that they occupied while receiving the payments.(4) Constrained housing allowances required the households to occupy housing which met certain "minimum standards". In contrast, for other groups, the housing standard specified that the total rent paid by the household must be at least equal to some proportion of the cost of "standard" housing. Two alternatives were used for the rent requirement i) a "low" rent of 0.7 of the cost of standard housing and ii) a "high" rent of 0.9 of the cost of standard housing.

Several further features of the demand experiment should be noted. The allowances were paid to a sufficiently small sample of householders in the designated areas so that no assessment could be made with respect to the effects of general housing allowances on either the level of rents or the supply of housing. Also, the allowances were paid for a period of only two years with assistance granted to households in the third year to help them obtain other suitable housing. This feature has the consequence that the experiments could not reveal the nature of households' responses to housing allowances which would be judged to be more permanent by the households.

3.2 The Supply Experiment(5)

The supply experiment was directed to determining the effects of housing allowances on the workings of housing markets. Although the housing allowances were comparable in design to those in the demand experiment, the experiment examined the following questions:

- When all eligible families are offered the opportunity to receive housing allowances, will landlords, developers, homeowners, mortgage lenders, real estate brokers and others accommodate the recipients in their attempts to improve their housing conditions? Or, as some predicted, will the price of housing simply increase without a corresponding improvement in housing?
- To what extent will housing allowances stimulate repairs, substantial rehabilitation or the construction of new units?
- As housing allowance recipients attempt to increase their housing consumption by moving, what neighbourhoods will they seek and which ones will they succeed in entering? What is

> the impact on the neighbourhoods they leave and enter? Will families move from the central city to the suburbs?

The supply experiment, in contrast to the demand experiment, paid housing allowances to all eligible households, whether rented or owned, in Green Bay, Wisconsin and South Bend, Indiana. These housing markets were chosen:

> To differ in certain ways, yet be typical of a substantial portion of markets throughout the nation. Brown County has a rapidly growing urban center, a relatively tight housing market, a good housing stock, and a very small minority population. St. Joseph County has a declining central city with a deteriorating housing stock, a minority population of average size but growing, and an excess supply of central city housing. (Allen et al., 1981, pp. 11-12)

The housing allowance for the supply experiment consisted of a housing gap system in which the allowance payment equalled the difference of a modest housing standard based on family size and location and 25 per cent of family income. In addition, the family must occupy standard housing in order to qualify. The allowances were quite substantial relative to income, ranging from 19 per cent of income for homeowners in the Wisconsin experiment to 44 per cent of income for renters in the Indiana experiment.

3.3 The Demand and Supply Experiments Compared

Several important differences should be noted in the design of the demand and supply experiments. First, the time period of the supply experiment was a full five years with a further five year commitment of payments to the participating households. In contrast, the demand experiment lasted only three years with analysis concluded after the second year.

The third year fulfilled two purposes: i) "to reduce confusion between participants' reactions to the experimental offers and their adjustment to the phase-out of the experiment (Friedman and Weinberg, 1982, p. 12) and ii) to aid households in entering other housing programs. The longer length of the supply experiment was necessitated by the belief that supply responds more slowly to market changes than does demand. The long period of the supply experiment would also be useful to the extent that demand adjustments require the household to move to another dwelling.

The other major difference between the demand and supply experiments occurred in their coverage. The demand experiments were confined to relatively small samples of eligible households in large markets, whereas, the supply experiments were open to all eligible households who met the housing standard in much smaller markets. Again, this design feature was necessitated by the purpose of the study. The aim of the supply experiment was to gain information about the supply response to a system of universal housing allowances. For this purpose, a sample of eligible households would be totally inappropriate. The experiment must simulate the pressures on the housing market of an allowance program which covers all households.

4.0 Assessment of Unconstrained Housing Allowances

The first step in analyzing the effects of demand policies is the consideration of the simplest form which is a totally unconstrained housing allowance. This analysis establishes a benchmark which indicates the basic effects of a demand augmenting policy.

In subsequent sections, attention is turned to the consequences of modifying the housing allowance program by the addition of requirements for minimum rental expenditures or mimimum quality standards for housing occupied by participating households. The most significant effects of these constraints are found with respect to adequacy of income and adequacy of housing. Each of these criteria are reviewed for the various forms of housing allowance. The other evaluation criteria are discussed with respect to all forms of housing allowance in general.

4.1 An Unrestricted Housing Allowance

Under an unrestricted housing allowance program, households qualify for assistance on the basis of income without any concern for quality of housing occupied by the household or the actual housing expenditures made by a household. This type of allowance is determined for a household of a given size, solely, by the relationship between its income and prevailing market rents.

In the absence of a minimum standard for housing, a demand program, using a housing cost index to determine the subsidy, becomes essentially a form of general income support identical to a negative income tax. As Aaron (1972) notes:

> The housing gap allowance is calculated according to a formula that is structurally indistinguishable from formulas tested in income maintenance experiments. The negative income tax formulas examined in the income maintenance experiments stipulated that households were to be paid a certain sum if they had no outside income (the guarantee) and that the payment was to be reduced by a certain fraction of income (the "benefit reduction" ratio). (p. 77)

Payments to any household under the general income maintenance can be expressed as

$$P_i = X - bY_i$$

where P_i is the payment to household i, X is the guarantee, b is the benefit reduction ratio, and Y_i is the household's current income. Similarly, Aaron (1972) states:

> The housing gap allowance assures each household some multiple of the estimated cost of standard housing C*, if the household has no income and reduces that guarantee by some fraction of income. (p. 77)

Thus, a housing allowance of this form would be expressed as

$$PH_i = C^* - hY_i$$

where PH_i is the housing allowance paid to household i, C* is the estimated cost of standard housing, h is the fraction by which the allowance is decreased in relation to income, and Y_i is the income of household i. The only difference is in the type of justification given for X and C*. Once these are set together with b and h, the schemes are identical in their effects. As Aaron (1972) concludes:

> The structure of housing allowances differs from that of negative income taxes only to the extent that conditions are imposed on housing allowances but not on negative income taxes. (p. 77)

4.2 The Workings of Unconstrained Demand Policies

It is useful to examine the workings of unconstrained demand policies to provide a basis of comparing their effects on the evaluation criteria with those of other policies, including various types of constrained demand policies. Such a comparison provides a basis for determining the ways in which the complementary policies, reviewed in this study, can contribute to achieving the goals identified with rent regulation.

Housing allowances work, in the first instance, by increasing the incomes, or spendable resources, of target households. This increase of resources for target households influences the rental housing market through

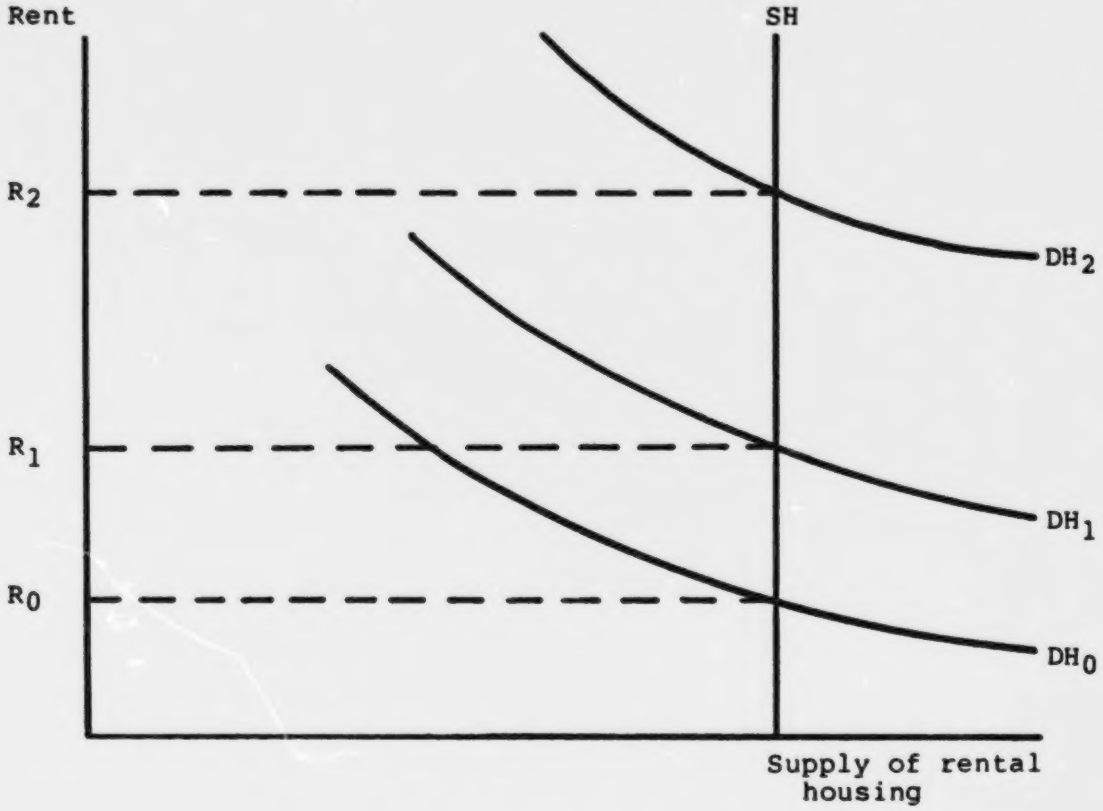
1) the effects of increased income on the housing expenditures of target households,
2) the effects of the increased housing expenditures on the rental housing market.

The effects on the demand for rental housing resulting from an unconstrained housing allowance program can be represented by a shift in the demand curve for rental housing from DH_0 to DH_1 in Figure 4.1a) and Figure 4.1b). The size of the shift depends on i) the amount of support for each assisted household, ii) the proportion of tenants that gain assistance and iii) the response of the recipient's demand for rental housing to the housing allowance. Factors i) and ii) depend on the design of the housing allowance program whereas iii) is determined by the behaviour of the assisted households. The nature of this response is discussed in Section 4.3 below.

As can be seen from the comparison of Figures 4.1a) and 4.1b) the impact of the program depends on the nature of the supply of rental housing. If the quantity of rental housing cannot be readily increased, as in Figure 4.1a), the unconstrained demand policy ends up raising rents without generating any increase in the supply of available rental housing. Thus, even though the tenant households were the proximate beneficiaries of the government policy, some of the

Figure 4.1a)

The Effects of Demand Programs: Fixed Supply



DH_0 : Demand for rental housing in absence of demand programs

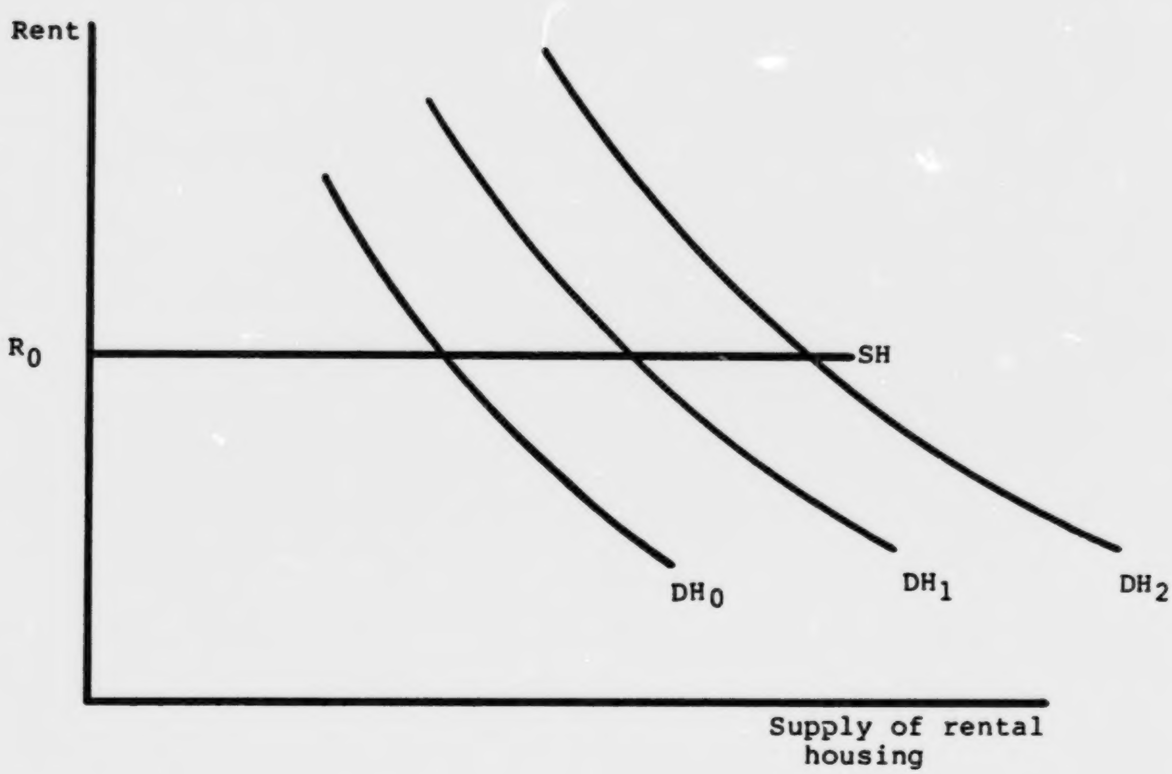
DH_1, DH_2: Demand for rental housing with demand programs

SH : Supply of rental housing

Figure 4.1b)

The Effects of Demand Programs: Responsive Supply

Rent



DH0 : Demand for rental housing in absence of demand programs

DH1, DH2: Demand for rental housing with demand programs

SH : Supply of rental housing

benefits will be passed to landlords in the form of higher rents.(6) In addition, tenants who do not receive the housing allowances also face higher rents. The amount which is transferred to landlords depends on the proportion of the benefits of housing allowances that households spend on housing. In addition, as the comparison of DH1 and DH2 shows, it also depends on the responsiveness of the demand by households for rental housing to the level of assistance. When the demand for housing is unresponsive to assistance as with DH_1, the rent increases from R_0 to R_1, a large increase from R_0 to R_2, as compared to the more responsive demand DH_2.

The most unfavourable setting for a demand program occurs when the supply of rental housing is completely fixed. Two factors reduce the relevance of this setting. First, the supply of rental housing is likely to be responsive to rental levels in the long run although it may be relatively unresponsive in the short run. Thus, even if the initial impact of the policy raises market rents, this effect will be offset by an increased supply of housing over time. Developers will respond to high rents by building more rental units. Second, the price increase will be greatest in a tight rental market. In a less tight housing market, some of the response will be taken up by decreased vacancy rates, which offset some of the tendency for rents to rise.(7)

The general framework developed above can be used for analyzing all types of housing allowances, whether constrained or unconstrained. The difference in the effects of different housing allowance programs arises from their impact upon the demand for housing. For any change in the demand for housing, the market effects which arise through the interaction with supply will be the same. Thus, the variants of housing allowances will be compared, first, with respect to their demand effects and the implications of any differences in the immediately following sections. The discussion of the market effects through the interaction with supply will be presented in Section 6.0 below.

4.3 Adequacy of Income: Unconstrained Housing Allowance

In pure theory, a program of general income support or its equivalent, an unconstrained housing allowance, can be designed to attain whatever income redistribution objectives policy makers desire to achieve. Establishment of a level of X or C* for each type of household establishes the eligibility of households whereas the setting of b determines the level of support at each level of household income. Indeed, much of the impetus of support for housing allowance programs arose from the view that existing "programs were considered inequitable because they served only a small fraction of the population eligible for housing assistance" (Friedman and Weinberg, 1981, p. 1).

In practice, an unconstrained housing allowance may not achieve its redistribution objective if all eligible households do not participate in the program. Failure to participate may arise from several reasons:

i) lack of awareness of program,

ii) unwillingness by potential beneficiaries to take the effort to establish eligibility and to enroll, and

iii) an unwillingness to accept assistance from the government.

The demand experiments under the Expermental Housing Allowance Program (EHAP) in the United States revealed that not all eligible households participated in housing allowance programs. The participation rate for housing allowances ranged from 90 per cent of eligible households in Phoenix to 78 per cent of eligible households in Pittsburg.

Special features of the EHAP experiments make it difficult to extrapolate these results to demand programs generally, or even to a housing allowance program which is judged by households to be permanent. Several factors appear to have lowered the participation rate under EHAP. The EHAP program was known to be temporary in that it offered benefits for only two years. In addition, household awareness of a program and its features could be expected to increase over time. Finally, the experimental needs of the program meant that participating households were required to undertake greater amounts of paperwork than would be expected under a universal housing allowance program. On the other hand, Straszheim (1981) observes with respect to the supply experiments that "households...received more assistance and friendlier treatment than would be typical in other welfare programs or likely in a universal housing allowance program" (p. 131). In contrast to the other factors influencing participation in the demand programs, this factor may have served to raise the participation rates of households.

These rates of participation in the unconstrained housing experiments are remarkably high relative to the participation rates experienced in other social programs. Bendick (1980) has surveyed a variety of forms of public assistance and found rates of participation ranging from a high of 90 per cent to a low of 4 per cent of those eligible, as presented in Table 4.1. The remarkable aspect of these data is the generally low rate of participation - an average of 46 per cent across all the programs. Thus, in comparison with social programs in general, a housing allowance without any restrictions appears to be an extremely effective means for delivering income assistance to target households. Only minor slippage occurs through failure to participate. A high degree of vertical and horizontal equity can be achieved among tenant households, according to the design of the program.

4.4 Adequacy of Housing: Unconstrained Housing Allowance

The adequacy of housing objective, as discussed in Chapter 3 above, reflects a concern by policy makers about the type of housing occupied by the households which are the targets of housing policy. By this criterion, the success of housing policy should be gauged by the improvement in the housing of the target group. At any given level of rent, the improvement in housing can be measured by the increased expenditure on housing by the target group. The best evidence on the effects of housing allowances on consumption of housing services comes from the Experimental Housing Allowance Program (EHAP) conducted in the United States.

An unrestricted housing allowance gives assistance to households, solely, on the basis of their current incomes, given existing levels of market rents. Thus, unrestricted housing allowances are virtually identical to pure income transfers. The empirical evidence available on the effects of housing allowances on housing consumption reinforces this

TABLE 4.1

Estimates of Participation in Selected Public Assistance Programs

Program	Eligible Population	Participating Units (percentage)
Aid to Families with Dependent Children	Female-headed families nationwide, 1967	63
	Female-headed families in the Chigaco area, 1967	74
	Female-headed families nationwide, 1970	90
	All eligibles nationwide, 1975	87
	All eligibles nationwide, 1976	74
Aid to Families with Dependent Children - Unemployed Fathers	Eligibles in the Chicago area, 1967	4
	Eligibles in states offering the program, 1971	15
	Eligibles in states offering the program, 1975	16
General assistance	Eligibles in the Chicago area, 1967	6
Supplemental Security Income/Aid to the Aged, Blind, and Disabled	Eligibles in the Chicago area, 1967	15
	Eligibles nationwide, 1976	60
Public assistance, unspecified	Eligibles in New York City, 1968	56
	Eligibles in New York City, 1970	60
	Eligibles in Jackson County, Oregon, 1970	44
Food stamps	Eligibles in Jackson County, Oregon, 1970	41
	Eligibles nationwide, 1974	38
	Eligibles nationwide, 1975	55
Free school lunch	Eligibles in Jackson County, Oregon, 1970	53
Experimental housing allowances	Eligibles approached by outreach workers in Phoenix and Pittsburgh, 1977	32
	Eligible renters in Green Bay and South Bend, 1977	44
	Eligible homeowners in Green Bay and South Bend, 1977	26
Circuit-breaker property tax relief	AFDC families in Michigan, 1973	12
	AFDC families in states offering benefits only to the elderly, 1974	69
	Eligibles in states offering benefits to persons of all ages, 1974	82
Average		46

SOURCE: Bendick, "Failure to enroll in public assistance programs," Social Work (July, 1980), p. 269.

view through comparison of income maintenance experiments with housing allowance experiments. Aaron reports that:

> Data from the Seattle and Denver income maintenance experiments indicate that 4.5 to 10.6 cents out of every assistance dollar go for housing. Data from the housing allowance demand experiment indicates that recipients of unconstrained payments spent 6 per cent on housing in Pittsburg and 19 per cent in Phoenix. (1981, p. 78)

Thus, an unrestricted housing allowance can be expected to have no more than minor effects on the housing consumption of the target households.

4.5 Effectiveness for Cost of Unconstrained Housing Allowances

The effectiveness for cost of unrestricted housing allowances can be assessed quite readily for both the adequacy of income and the adequacy of housing objectives. Unrestricted housing allowances can be directed toward a target group of households with little spill-over to other groups and with a high coverage of the target group. The only source of slippage arises from tax administrative expenses required to implement the program. Thus, unrestricted housing allowances are extremely effective instruments for attaining the adequacy of income objective.

The adequacy of housing objective would be advanced if a substantial proportion of the allowances were spent on improved housing. A careful assessment from this perspective would have to distinguish between increased expenditures on housing and the improvement in the housing which results from this expenditure. In the case of unrestricted housing allowances, such a distinction is unnecessary. The evidence suggests that only a minor proportion of the allowances was spent on housing. Unrestricted housing allowances are ineffective from the adequacy of housing perspective. Both the total value of the allowances and any administrative cost have been expended with little effect on housing expenditures by the target group.

5.0 Assessment of Constrained Housing Allowances

As discussed earlier, most housing allowance programs, whether actual, experimental or proposed, include some constraint, either upon the receipt of assistance or upon the expenditure of the assistance, once received. In some dimensions, the addition of constraints does not alter the analysis of unconstrained housing presented above. In others, the consequences of the constraint are important enough that the conclusions of the analysis are substantially different. The following sections discuss the modifications to the analysis of adequacy of income and adequacy of housing which arise from the introduction of constraints into housing allowances.

The constraint built into housing allowances can take a variety of forms. The constraint can determine either the level of assistance to households or the eligibility of households for any assistance. Moreover, the criteria for establishing eligibility can be an expenditure requirement or a housing quality requirement. On the basis of this classification, three separate categories of constrained housing allowances can be identified as shown in Table 4.2 below. A sufficient difference exists between constraints on eligibility and constraints on the level of assistance that these

TABLE 4.2

Types of Rental Constraints

Policy	Type of Constraint	Variable determining Constraint
Assistance:		
Percent of rent paid	determines level of assistance	actual rent payment up to a maximum proportion of income
Eligibility:		
Minimum standards	determines eligibility	physical quality of housing
Eligibility:		
Minimum rent	determines eligibility	payment of rent in excess of specified minimum

categories will be considered separately in the analysis that follows.

5.1 The Workings of a Rent Constrained Program

A housing allowance program, with a constraint on the level of assistance to be no more than the level of actual rent, can be compared with an unconstrained housing allowance program to illustrate the consequences of this constraint on the assistance paid to households.(8) In form, the two programs would appear to be identical:

Unconstrained:

$$PH_i = a(C^* - hY_i)$$

Assistance constrained by actual rent paid:

$$PH_i = a(R_i - hY_i) \qquad R_i < R^*$$

where the variables are defined as follows:

PH_i - housing assistance paid to household i,

Y_i - income of household i,

h - fraction by which the allowance is decreased in relation to income,

a - percentage of gap made up by housing allowance,

C^* - the estimated cost of standard housing,

R_i - the rent paid by household i, and

R^* - the maximum rent for calculating PH_i.

The difference between the two programs occurs because C^*, in the unconstrained program, represents the representative cost of rent and is unrelated to actual expenditures, whereas R_i, in the unconstrained program, represents the actual rental expenditures of the household.

The unconstrained program used in the example could, for example, assign a value for C* of $300 per month and a value for h of 0.25. The per cent of rent plan assigns the same value to h and sets R* at $300 as the maximum rent for the purpose of calculating the monthly assistance for any household.

Table 4.3 compares the assistance paid to various households according to income and actual rental payments under the two plans. As can be seen, the level of assistance under the constrained plan is the same as the unconstrained plan at all levels of income for households that spend at least $300 per month on rent. The pattern is different, however, for households spending less than $300 per month for rent. If, for example, a household with no income spends just $150 a month on rent, it will receive the same benefits as households spending more on rent but with incomes exceeding $600 per month. In addition, the assistance given to a household spending $150 per month on rent is quite insensitive to income. Such a household receives $75 per month regardless of income over a range of income from $0 to $600 per month.

5.2 Adequacy of Income: Rent Constraint

The introduction of actual rent as a constraint in the design of a housing allowance adds an additional criterion to the determination of a household's level of assistance through housing allowances. The assistance depends on actual rent paid, in addition to income. This change alters substantially the payment which is made to those households which choose to spend little on housing.

TABLE 4.3

Comparison of Assistance to Tenants Under Unconstrained and Actual Rent Constraint Programs

Monthly income	Assistance under unconstrained program (all levels of rent)	Assistance under actual rent constraint Rent paid				
		150	200	250	300	350
0	150	75	100	125	150	150
200	125	75	100	125	125	125
400	100	75	100	100	100	100
600	75	75	75	75	75	75
800	50	50	50	50	50	50
1000	25	25	25	25	25	25
1200	0	0	0	0	0	0

$PH_i = 150 - .125\ Y_i$ $PH_i = .5\ (R_i - .25Y)$

R_i - calculated on the basis of actual rent or \$300, whichever is less.

The adequacy of income effects, it is recalled from Chapter 3, can be expressed in terms of horizontal and vertical equity. Horizontal equity refers to the degree to which the program gives equal assistance to households with equal income. Vertical equity refers, in contrast, to the distribution of benefits among households according to their different levels of income. It is measured by comparing the benefits received by households at one level of income with the benefits received by households at another level of income.

The effects of the actual rent constraint on horizontal equity can be seen by comparing households at the same level of income. In Table 4.3, the assistance to households with lower incomes differ substantially according to the actual rent paid by the household. At an income level of $0 per month, the assistance ranges from $75 a month to $150 a month to households paying rent of $150 a month to $350 a month, respectively. Comparison of the differences in Table 4.3 reveals that those differences are most pronounced across households with low levels of income. Thus, the introduction of a constraint on assistance to the amount of actual rent paid reduces horizontal equity in the program. Equals in terms of income are not treated equally. The benefit received by a household depends on the level of housing expenditure.

The change in the design of the program to include rent as a criterion for assistance also affects vertical equity of the program. Suppose the unconstrained program represents that distribution of benefits that would be judged as vertically equitable. As can be seen from Table 4.3, the actual rent constraint changes the vertical equity of the housing program. Some households which have higher income gain benefits which are larger than those gained by households with lower income. In Table 4.3, all households with income of $400 per month which spend at least $200 per month on rent gain more under the program than households with income of $0 which spend only $150 per month on rent. The actual rent constraint changes the pattern of distribution of benefits. Thus, if the distribution of benefits, in absence of a constraint, reflects the intended degree of vertical equity, the introduction of an actual rent constraint reduces the degree of vertical equity.

5.3 Adequacy of Housing: Rent Constraint

The adequacy of housing objectives, as shown in Chapter 3, measures the degree to which a housing program increases the quality or quantity of the housing occupied by target groups of households. As shown in Section 4.5 of this chapter, an unconstrained housing allowance causes only minor changes in the housing expenditures of the households.

The unconstrained transfer can be considered the same as an increase in income without any effective change in the price of rental housing facing the household. The substitution of actual rent for prevailing market rent in the formula for determining benefits changes the effective price of housing for the assisted household. This effect can be seen from Table 4.3. Consider a household with income of $200 per month which spends $150 per month on rent. Under the unconstrained housing allowance, this household receives $125 per month of assistance, regardless of its actual rent.

If it decides, for example, to move from housing at $150 per month to housing at $200 per month, it must pay $50 additional rent and have $50 less to spend on other goods and services.

In contrast, if this household spent $150 on rent under the expenditure constrained allowance it would receive only $75 per month. The low level of its actual rent prevents it from receiving the maximum benefit. If, under this program, it decides to move from housing at $150 per month to housing at $200 per month it gains $25 income in assistance. Even though it pays $50 in additional rent, it need spend only $25 less on other goods and services. As a consequence, the effective costs to the household of increasing its housing expenditures are $25 for each $50 rent actually paid. The effective rent to the household is lowered.

This difference in effective rent under the actual rent constrained and the unconstrained housing allowance programs makes a substantial difference to their performance with respect to the adequacy of housing goal. The unconstrained housing allowance leaves unchanged the marginal price of rental housing that faces the household. The introduction of an actual rent constraint, on the other hand, reduces the marginal cost of housing for all households below the ceiling to allowable rent for the purpose of assistance. Target households which are below the assistance ceiling have a greater incentive to spend more on housing than they would with an unconstrained allowance program.

The effects on housing expenditures of the incentives arising from an expenditure constraint depend on three factors:

1) the number of households affected by the constraint,

2) the size of the incentive caused by the constraint,

3) the response of the affected households to the constraint.

The first two factors are elements in the design of the program. The only behavioural variable is the response of affected households. The evidence from the EHAP experiment suggests that the elasticity of demand for rental housing is likely to be 0.5 or less.(9) This means that a one percent change in the cost of housing at the margin leads to a one-half percent change in quantity of rental housing demanded. Thus, an expenditure constrained housing allowance which provides a subsidy equal to twenty-five per cent of actual rent, would induce a twelve and one-half per cent increase in rental expenditures by households receiving assistance.

5.4 Effectiveness for Cost: Rent Constraint

A rent constraint has quite substantial effects on the performance of a housing allowance with respect to both adequacy of income and adequacy of housing. The presence of the rent constraint does not affect the ability to provide benefits to the target group, though, as seen in Section 4.3 above, it changes the distribution of benefits to make them depend on the rental costs incurred by households. On the other hand, a rent constraint is more effective than an unconstrained allowance in increasing the level of expenditures on rental housing. As already discussed in Section 4.4, the rent constraint lowers the effective price of housing for assisted households and induces them to consume more housing.

The evidence from the Experimental Housing Allowance Program suggests an elasticity of the demand for rental housing of one-half -- a one per cent decrease in the price of housing leads to a one-half per cent increase in the demand for housing. Thus, a housing allowance with benefits set at twenty-five per cent of rent could be expected to induce, at a maximum, a twelve and one-half per cent increase in housing expenditure.

5.5 The Workings of Housing Allowances with Eligibility Constraints

So far, the only constraint on housing allowances to be considered has been a constraint on the amount of assistance. Another type of constraint is one that determines eligibility for programs. Eligibility constraints set minimum standards which must be satisfied in order for a household to gain any benefits under a housing allowance program. Two separate constraints which were examined in the EHAP experiment can be used to represent the types of constraints which might be integrated into actual housing allowance programs. One constraint took the form of a quality standard which required households to occupy housing which satisfied specified physical characteristics in order to receive assistance. The other established minimum levels of rent which households must pay in order to receive benefits.

The first stage in the workings of demand augmenting policies falls on the housing expenditures of target households. The overall response of housing demand to a housing allowance which has a minimum housing requirement depends on the response of three groups:

i) those that meet the requirement in advance,

ii) those that adjust their expenditures so as to meet the requirements,

iii) those that fail to meet the requirements of the program.

A constrained demand program is essentially identical to an unconstrained policy for the first group mentioned above, and their response is likely to be the same. The response of the second group is less predictable. For some households in the second group, the added expenditure required to qualify for the program will be less than the amount they would spend under an unconstrained program. The response by these households is likely to be comparable to that of the group which qualified in advance. Others in the second group will increase their spending on housing more than they otherwise would due to the constraint, in order to qualify for the housing allowance. The final group, because it would continue not to qualify in any event, would neither adjust its expenditures nor gain any benefits from the program.

The overall effects on housing demand of a constrained program compared to an unconstrained program depend on the responses of the second and third group. The first group qualifies without any need to adjust housing expenditures under both programs. The second group must increase housing expenditures in order to qualify for the constrained housing allowance. The third group does not gain any benefit under the constrained program, whereas, it would have in the absence of the constraint. Its expenditure on housing will be less under the constrained program because of the loss of the benefit. The net effect will depend on the value of the subsidy under the demand program and the cost of meeting the constraint to households that fail to qualify initially. The value of the subsidy determines the benefit to households from qualifying to meet the constraint. Households will compare it with the costs of meeting the constraint in making their decisions to qualify.

The addition of an eligibility constraint to the housing allowance alters the demand for, but not, the supply of rental housing. As should be clear, the demand for housing could be increased or decreased relative to an unconstrained housing allowance, depending on the exact design of the program and the response by households. In any case, the introduction of a constrained housing allowance will cause some increase in the demand for rental housing even though it may be less than for an unconstrained program.

5.6 Adequacy of Income: Eligibility Constraint

The presence of a quantity constraint can substantially alter the effects of a housing allowance on the goal of adequacy of income. In an unconstrained program, all households in the relevant range of income levels qualify for assistance. The existence of a minimum standard for eligibility means that some households may forego the benefits by failing to improve their housing up to the minimum standard. Determination of the effects on income distribution of a housing allowance with a minimum housing standard are complicated by the fact that some households meet the standards by their housing prior to receiving assistance, whereas, others do not. The question, thus, arises as to how much of a deviation from horizontal and vertical equity is caused by imposing a constraint on a housing allowance program?

For the households which already meet the housing standard, participation is to be limited only by considerations such as lack of knowledge, unwillingness to fulfill administrative procedures or reluctance to accept payments from government. A more difficult choice faces the households which do not meet the housing standards. One alternative for them is to improve their housing so as to meet the standards by moving to alternative housing or by modifying their existing housing. Maintaining the same quality housing causes them to forego any benefits from the housing allowance.

As discussed earlier, the participation rates in unconstrained housing allowance programs were high relative to those achieved in social programs, in general. The presence of a constraint, either in the form of required expenditures on rent or a minimum housing requirement, reduces the rate of participation drastically. Table 4.4 shows the effects of eligibility constraints as revealed by the demand experiment. With no restrictions, participation rates fall within the range of 78 to 90 per cent, depending on the program and the location. Programs with minimum quality standards experienced participation rates as low as 30 per cent. Over all constrained programs, the average participation rates were 41 per cent in Pittsburg and 49 per cent in Phoenix. Earlier in Section 4.3, the participation rates in the unconstrained programs were compared with data assembled by Bendick with respect to a variety of social programs. The average participation rate of 46% in all

TABLE 4.4

Participation Rates in the Demand Experiments, by Program Type

	Pittsburg	Phoenix
No restrictions		
Unconstrained	78	87
Per cent of rent	82	90
Minimum quality standard		
Minimum standards	30	45
Low minimum rent	60	61
High minimum rent	42	44
Average minimum quality restrictions	41	49

SOURCE: Straszheim, p. 122 from Stephen D. Kennedy and Jean MacMillan, Draft Report on Participation under Alternative Housing Allowance Programs: Evidence from the Housing Allowance Demand Experience (Abt, October, 1979), pp. 24-25.

social programs reviewed by Bendick is roughly comparable to the participation rates found in the restricted housing programs found in Pittsburg and Phoenix. Nevertheless, the constrained programs experienced participation rates substantially below those of the unconstrained programs.

The evidence, cited above, demonstrates that eligibility constraints lower participation rates substantially. The distribution effects of this reduced participation also depend on the patterns of participation across different types of households. Evidence from the demand experiment provides a comprehensive profile of the enrollment rates of households that strongly suggests that the characteristics of households were an important determinant of participation:

> Among socio-economic groups, enrollment rates were slightly higher for households whose members were younger, that had moved more often in the past three years, or that received welfare or food stamps. With the exception of slightly lower enrollment rates for the lowest income class, income appeared uncorrelated with enrollment rates. (Straszheim, 1981, p. 122)

The demand experiment also produced evidence on the sensitivity of enrollment to the size of the income transfer:

> The size of the income transfer affected enrollment rates. Enrollment rates were about 67 percent for households that were told to expect a subsidy of only $10, about 87 percent for households that would receive $31 to $50 transfers, and only marginally higher for those receiving larger expected transfers. (Straszheim, p. 123)

The supply experiment, as discussed above, was designed to simulate the market response by assuring assistance to a proportion of households which would approximate the coverage under an actual housing allowance program. Nevertheless, the supply experiments do provide further useful evidence in the form of descriptive statistics about the redistributive effects of housing allowances. The supply experiments differ from the demand experiments in a number of dimensions which can be expected to affect participation rates. First, mass publicity was used to make the public aware of the program in contrast to the individual outreach and interviewing in the demand experiments (Straszheim, 1981, p. 131). Further, the supply experiment was based on a less stringent housing standard than used in the demand experiments. Finally, the supply experiment was directed to all eligible households in housing markets, rather than being confined to just a sample, as in the case of the demand experiment. Each of these factors probably contributed to raise the participation rates above those which would have occured under the conditions of the demand experiment.

Table 4.5 presents the characteristics of the participants in the supply experiment. As in the demand experiment, the elderly are under-represented. While the data shows that enrollment tended to be inversely related to income in general, though, low participation rates are found for the very lowest income groups. The figures on overall participation show that, despite the favourable features of the supply experiment, the actual participation rates remained very low. In neither site of the supply experiment did the participation rates exceed 45 percent of eligible households.

The preceding discussion answers two questions. How much do eligibility constraints affect participation? Who participates? The answers to these questions contribute to

TABLE 4.5

Profile of Participants in the Supply Experiment, 1978
(Percent unless otherwise specified)

Household characteristic	Brown County, Wisconsin Eligible population	Brown County, Wisconsin Participants	St. Joseph County, Ind. Eligible population	St. Joseph County, Ind. Participants
Tenure				
Own	53	31	70	54
Rent	47	69	30	46
Age of household head				
Under 62	58	63	46	54
62 or over	42	37	54	46
Race of household head				
White	97	97	83	75
Other	3	3	17	25
Size of household				
1	23	43	30	45
2	27	26	34	26
3-4	25	24	22	21
5-6	16	6	9	6
7 or more	9	2	5	1
Annual gross income 1978 (dollars)				
Owners	n.a.	5,490	n.a.	4,604
Renters	n.a.	4,646	n.a.	3,467

SOURCES: Straszheim (1981) from p. 132. Eligible population from Lawrence W. Kozimor, *Eligibility and Enrollment in the Housing Allowance Program: Brown and St. Joseph Counties through Year Two*, Rand WN-9816-HUD (Rand Corp., 1978), pp. 17, 19, 96, 100, 106, 133, 143. Participants from Rand Corporation, *Fifth Annual Report of the Housing Assistance Supply Experiment* (Rand, June 1979), pp. 21, 23.

the assessment of the equity effects of imposing constraints on eligibility.

The reduced participation which results from eligibility constraints affects horizontal equity. The principle of horizontal equity requires that the program reaches the entire target group. To the extent that some members of the target group do not participate means equals are not being treated equally. Even though an unconstrained program does not assure complete participation, the types of constraints which were introduced in the EHAP experiments have drastic effects on participation, as illustrated by the fall in participation from approximately 90 per cent to less than 50 per cent.

The introduction of the eligibility constraints does not have an even effect on participation rates of different groups. Households which are well-housed bear minor, if any costs, in meeting the requirements. Similarly, households which would be mobile in absence of the program are also able to adjust at little expense. The evidence suggests that the elderly and the very poor are among the least likely to fulfill the eligibility requirements. While such a pattern of participation appears to conflict with horizontal equity, it also conflicts with vertical equity. Assistance is based on other criteria than income. As a consequence, some households with relatively high incomes can qualify for assistance while other households with lower incomes do not.

5.7 Adequacy of Housing: Eligibility Constraint

As discussed in Chapter 3, the adequacy of housing objective reflects a concern by policy makers with the quality of housing occupied by the target groups. The introduction of mimimum standards, whether in terms of quality or expenditure, seemingly contributes to this goal. Such a supposition would be correct if participation by the target group was unaffected by the standard. On the other hand, if a housing standard discourages participation, its consequences could be counterproductive in terms of the adequacy of housing objectives.

The adequacy of income effects of an eligibility constraint were examined in terms of two questions:

1) How do constraints affect participation?
2) Who participates?

Similarly, the evidence of the effects of eligibility constraints on adequacy of housing can be summarized in terms of another question: what factors influence participation? For the group that qualifies through their existing housing, the answer is quite simple. They would be expected to qualify at rates similar to households participating in unconstrained programs. The crucial question thus becomes the behaviour of households which would be eligible except for the quality of their existing housing.

What factors would shape the decisions of eligible households living in substandard housing? The choice involves a trade-off between the costs of meeting the minimum standard and the additional income to be gained from the housing allowance. The degree to which the household's current housing falls short of the minimum standard determines the costs. Similarly, the household's current income, together with the design of the system of housing allowances, determine the benefits from the program. On theoretical grounds, it is not possible to predict the patterns of participation in a housing allowance program by income group. While the very poor clearly have the most to benefit from in terms of income support, this group also is the most likely to occupy substandard housing and to have to incur the greatest expense in making their housing meet the standard.

The EHAP experiments supply useful information about the participation of different types of households in housing allowance programs. Evidence on participation was derived primarily through the study of household behaviour under the demand experiment but some useful information was also developed from the supply experiments.

Straszheim (1981, pp. 126-127) analyzes the findings of the demand experiment. He observes that a household's decision to upgrade their housing to meet the housing standard is determined by the valuation of additional housing and not by the proportion of income already spent on housing. A further consideration influencing the choice are the relocation and transactions costs of finding adequate housing. In some cases, these costs can be avoided by bargaining with a landlord. Changing one's residence, on the other hand, may impose substantial psychic costs in terms of adjusting to a new neighbourhood and its environment.

Straszheim summarizes the results from the EHAP demand experiment which were used by Kennedy and MacMillan (K-M) to analyze the participation for households that were eligible for a housing allowance program except for the failure of their initial housing to meet the minimum housing standard. The K-M study estimated a statistical equation to show the separate effects of:

1) the size of payment,

2) the difference between the quality of the household's current housing and the quality required to meet the minimum standard,

3) the household's normal probability of moving.

(Straszheim, 1981, pp. 127-29)

With respect to the first two factors, Straszheim reports that increasing payment levels only had modest effects on participation, but:

> Households whose housing quality was furthest from the minimum standards required in the housing gap plans were least likely to participate. (p. 129)

The final factor, the probability of moving, requires further discussion. Households vary with respect to the probability that they would move in any period, in the absence of a housing allowance. The fact that a household would move for other reasons makes it easier to conform to the standards required for the program because it would bear the costs of the move in any case. It must weigh only the additional costs of finding suitable accommodation against the benefits gained from the program. Households which did not intend to move face a more difficult choice. They must balance the total cost of the move against the benefits of the move. As K-M expected, households that were judged likely to move had a higher probability of participation than other households.

While the evidence is indicative of the factors which influence participation in a constrained housing allowance program, it does not permit any speculation about the effects of a particular program. These effects depend on:

1) the type of constraint embodied in the program,

2) the benefits to be gained from meeting the constraint,

3) the condition of the housing occupied by the target group.

The evidence from the experiments do suggest that eligibility requirements can have a substantial influence on participation. The effects of eligibility requirements on housing quality can be measured by the change in quality of housing of that group which i) did not qualify prior to the program and ii) altered their housing in order to qualify. The evidence suggests that many households can adjust their housing to qualify with little expenditure. On the other hand, the evidence also suggests that those households that choose not to qualify are those with low incomes and those that are most poorly housed.

5.8 Effectiveness for Cost: Eligibility Constraint

An eligibility constraint has quite different effects with respect to effectiveness for cost than does a rental constraint. The rent constraint provides assistance to exactly the same households as an unconstrained allowance but their benefits depend on actual rent. In contrast, an eligibility requirement excludes some households in the target group from receiving benefits because their housing fails to meet the standard. Nevertheless, the eligibility constraint does nothing to affect the ability to confine benefits within the target group so that no spill-over occurs. The need to establish eligibility for benefits does add to the administrative costs of the program.

The eligibility constraint complicates the analysis of the effectiveness of cost with respect to the adequacy of housing objectives. The problem arises because the effects depend on the height of the constraint. With a very low constraint, most households qualify on the basis of their original housing and, as a result, respond as they would to an unconstrained allowance. As the height of the constraint rises, fewer households qualify initially. Households will increase their housing expenditures somewhat in order to qualify. So at some stage, a constraint has a maximum effect on housing expenditure. Beyond that stage, raising the constraint reduces the number of households that choose to qualify. As a result, after this point, the constrained allowance causes fewer households to adjust their housing expenditures.

The overall impact on housing expenditures resulting from a constrained housing allowance depends on

i) the proportion of households that qualify without adjusting their housing expenditures,

ii) the proportion of households that adjust their expenditures in order to qualify,

iii) the households that choose not to qualify.

Group i) receives the allowance but does not need to adjust its housing expenditures, whereas, group ii) must increase its housing expenditures to gain assistance. The larger is group ii) and the smaller is group i), the more cost efficient will be the constrained housing allowance, in terms of achieving adequacy of housing. The relative size of these groups depends on a number of aspects of program design including size of benefits for each income group and the nature of the constraint. Moreover, the effectiveness of the program will also depend on the quality of housing initally occupied by the target group.

6.0 Housing Allowances and the Workings of the Rental Housing Market

The redistributive effects of a demand policy would be nullified to the degree that the increased expenditures by recipients on housing raises the prevailing level of market rents. The fear of such an unfavourable impact has been a source of criticism of housing allowances. Hulchanski (1983), for example, declares:

> The most serious concern about a full-scale shelter allowance program is rent inflation.... because they directly and immediately stimulate demand rather than supply, permit more of the population to compete for the existing rental units. Unless there is a healthy vacancy rate and a supply of new affordable rental units coming on stream, normal market dynamics will lead to increased rent levels in general, i.e., for all tenants. The shelter allowance subsidy, in this case, could simply pass through the tenant to the landlord. (p. 46)

It was precisely this concern which motivated the supply element of the EHAP experiments in the United States. The supply experiments were designed so as to ensure that the proportion of households that received benefits in the markets that were studied approximated the proportions which would receive benefits under an actual housing allowance program.

The findings from the supply experiments were quite unexpected:

> There appear to have been no market effects, that is, the shift in market demand functions in the two experimental sites appears to have had no effect on

> housing units in either market or in any submarket. (Mills and Sullivan, p. 254)

The findings from the experimental sites were also compared with national and regional rent increases. Mills and Sullivan concluded:

> For each period for which data are available, rent inflation was less in both Brown and St. Joseph counties than in the national and regional averages. (p. 254)

The reasons for the lack of any impact of housing allowances can be attributed to a weak response of housing demand to the housing allowances or to a very responsive supply of housing (Mills and Sullivan, p. 256). Barnett and Lowry (1979) offered one demand explanation and three supply explanations. The demand explanation suggests that the responsiveness of housing demand to increases in income are smaller than have been previously expected. The supply explanations can be summarized as follows:

- the gradual phasing in of the programs permitted supply side adjustments without an impact on rents
- many dwellings could be improved to meet housing standards at relatively minor expense
- increases in demand for housing do not increase market rents to any large degree until the stock of vacant units has been exhausted. (Mills and Sullivan, pp. 256-60)

Steele (1985b) also examines evidence on the market effects of housing allowances. In addition, she suggests a further way in which the benefits of housing allowances could be dissipated in higher rents:

> Housing allowances may not increase the demand for housing, but the landlords of recipients exploit any limited monopoly power may have to increase

> rents. For example, the landlord of an elderly widow, knowing she has increased income derived from the allowance program and knowing that for her the cost of moving, broadly interpreted, is very great, may increase her rent. He thus gets increased revenue without the turnover costs usually associated with it. (p. 17)

Steele (1985b) uses evidence from a housing allowance program in Manitoba with respect to recipients who did not move in the first eighteen months of the program and concluded:

> In the case of both family and elderly recipients the rate of increase was less than the rate of rent inflation as indicated by the rental component of the CPI. Very clearly landlords did not exploit the housing allowance. Very clearly the housing allowances did not simply pass through to the landlord. (p. 18)

This evidence suggests the problem of exploitation by landlords is likely to be minor.

Steele (1985b) also suggests that the market impacts of housing allowances will also be small:

> Impressive and yet important evidence on rent inflation is found in the patterns of program costs over time. If the housing allowance programs induced market rents, overall, to rise, or market rents in the low end of the market to do so, or if the programs induced landlords to exploit allowance tenants, program costs would be expected to rise greatly over time. (p. 18)

Steele then compares the overall costs of programs over time and concludes:

> But [in data shown] they did not. Indeed they rose by about the rate of inflation. (p. 18)

6.1 Expectations of Full Programs

Hulchanski (1983) is extremely critical of the interpretations of the evidence on impacts on rent which extrapolate predictions about the effects of a full housing allowance program:

> Unfortunately, some of the evaluations of the U.S. supply experiment automatically conclude that a national program will also be successful (i.e., have minimum impact on the housing market). This conclusion is often supported by reference to the British program, which also has had a minimum impact in terms of recent inflation. Neither program seems to have had a detrimental impact on local housing markets. (p. 24)

He argues that these conclusions derived from experiments cannot be applied to a national program because of their limited coverage:

> As of 1977, the U.S. program only assisted 21,500 households across 12 EHAP communities, many of which had high vacancy rates. In Britain, only 200 households were participating in the Rent Allowance Program across the entire nation. It appears that the U.S....program will have assisted a total of 30,000 households, and not all at the same time, during its decade of existence. This is a large number for an experiment but it is insignificant in terms of measuring market impacts. (pp. 24-25)

While Hulchanski is quite correct in arguing that the numbers involved in the EHAP experiments were small, his criticism overlooks an important feature of the designs of the experiments. The demand experiments did cover only a small proportion of their respective housing markets. The supply experiments, in contrast, were designed specifically to measure the impact of a "saturation" program in which the proportion of households would approximate the proportion in an actual program. As Mills and Sullivan (1981) report:

> In Brown County, 16 percent of renters received program payments in 1978, and payments equalled 7 percent of countywide rent payments. In St. Joseph County, 12 percent of renters received payments,

> and payments equalled 6 percent of countywide rent payments. (p. 254)

Moreover they argue:

> The data just cited imply that the additions to incomes of renters from the program were substantial in both counties and that the effect on housing rents, at least in certain submarkets, might have been considerable. Whatever effect was to result had presumably materialized by 1978. Enrollments had stabilized by then, and the largest effects probably occurred in the short run, before supplies had had a chance to adjust. (p. 254)

Thus, it appears the two supply experiments appear to have been designed to avoid the criticism levied by Hulchanski that the numbers involved in the experiments were too small to simulate an actual housing allowance program.

Hulchanski also argues that the experiments failed to capture the impact of a housing allowance on a tight housing market. He cites Clayton's (1980) argument:

> That the two markets covered by MASSE were not representative of the generally tight rental markets which prevail in many Canadian centres. The two markets, Brown County and St. Joseph County, had vacancy rates of 5.1 percent and 10.6 percent respectively. This compares with the high 5.3 percent (London), low of .1 percemt (Vancouver and Victoria) and average vacancy rate in Canadian metropolitan areas of 2.5 percent... At best, the MASSE experience appears to be relevant only to soft markets in Canada. (p. 13)

This argument does create some concern about the current applicability of the experimental data for many areas in Ontario. Still, the significant finding of the experiment did not relate to the impact of increased demand on the rental housing market. The housing allowances influenced the demand for housing to only a limited degree. The condition of the housing market does not matter if housing allowances have only minor effects on the demand for rental housing. The problem might be exacerbated if the rental allowance produced a greater incentive for housing expenditure by havings its benefits tied to actual housing expenditures.

7.0 Rent Gouging

A demand augmenting policy, by itself, can do nothing to prevent rent gouging of the type where an uninformed household pays higher than prevailing market rents for rental accommodation. Such a program can, at best, ameliorate the burden of a tenant household that is being gouged by their landlord by increasing the level of assistance to reflect the level of rent.

Although housing allowances can serve to insulate households from rent gouging, this rationale is rarely used for their defence. Presumably, transferring the cost of gouging to taxpayers is not seen as the most constructive solution to the problem. Direct restrictions of gouging may be preferred. However, if the problem of rent gouging in response to housing allowances is minor, the cost of maintaining effective restrictions may not be warranted, particularly if the burden for the most vulnerable tenant households is alleviated by a general subsidy program such as a housing allowance.

8.0 Security of Tenure

Demand programs offer households additional security of tenure in a number of ways. In a very general way, a policy which increases household income makes any level of housing more affordable. The effects of some demand programs go beyond this effect to protect the household from insecurity of tenure resulting from periods of decreased income and from unfavourable housing market developments.

Most forms of demand subsidies, including housing allowances, depend on the relationship between income and some standard of rental expenditure. Decreases in income, depending on the period over which the income criterion is calculated, trigger an adjustment in the assistance received by the household. This increased benefit makes it easier for the household to maintain its current accommodation despite its decreased income.

A demand program can also help to preserve security of tenure in the face of escalating rents. In effect, such an increase in rent levels represents a decrease in real income to the household. Unrestricted housing allowances which depend on prevailing housing costs can also be designed to respond to changes in market rents. An allowance indexed to market rents is likely, however, to be adjusted to reflect local conditions only with some delay.

9.0 Economic Efficiency

An unrestricted housing allowance has relatively minor effects on economic efficiency compared to most other housing programs. Any effects of unrestricted housing allowances on information and transactions costs are likely to be insignificant. The only effect might arise because households receiving housing allowances will be able to afford a wide range of choices and will not have to incur as great information and transactions costs in order to find suitable accommodation.

Unrestricted housing allowance programs are also efficient with respect to housing use because they are based on representative housing costs. They are, in effect, an unconstrained income transfer and can be spent in any way the household chooses. As a consequence, the household's valuation of the transfer is higher than it would be if constrained.

A further dimension of economic efficiency is the efficiency with which the housing stock is used. A program leads to inefficient use of housing to the extent that households face rental housing prices which do not reflect the actual costs of supplying the housing. Households overconsume housing when the costs to them of using housing are less than the actual costs of supplying the housing. With an unrestricted housing allowance, the benefits to the household depend on the representative costs of housing, but not on the actual housing expenses of the households. Thus, the household's costs of rental housing are not directly subsidized and reflect the actual costs of supplying the housing. The design of an unrestricted housing allowance does not, as a consequence, provide any incentive for the household to overconsume housing.

The introduction of either an expenditure or quantity constraint into a housing allowance program can have substantial effects with respect to economic efficiency. The effects of each of these constraints are sufficiently different from one another that they should be treated separately.

An expenditure constraint ties the assistance received by a household to some proportion of the actual rental payments made by that household. As discussed earlier in Section 5.3, this type of housing allowance reduces the effective rent paid by the household. The expenditure constraint converts the housing allowance from a pure income transfer into a subsidy to consumption of rental housing.

Such a subsidy to rental consumption has a number of detrimental effects in terms of economic efficiency. Households are induced to consume more rental housing than they would otherwise. With the housing subsidy, households will have a greater incentive to occupy larger and better quality housing units. Moreover, the presence of a subsidy to rental housing will alter decisions by households with respect to renting versus buying their accommodation.

Economic efficiency requires that people's valuation at the margin of what they consume equal the costs at the margin, of producing that consumption. The presence of a subsidy prevents attainment of that equality. Recipients of expenditure constrained allowances do not value their additional housing as much as its costs because they do not bear the whole cost of this housing. Thus, an expenditure constrained housing allowance leads to a loss of economic efficiency relative to other means of transferring income to the target groups.

The analysis of housing allowances with a quantity constraint is more complicated. For those households which qualify in advance, the quantity constraint does not have any effects on efficiency. Other households, however, are required to improve their housing in order to qualify. The decision which must be made by these households requires the comparison of the additional expenditure on housing that they are required to undertake with the benefits of i) better quality housing and ii) the assistance received from the allowance. In these circumstances, the value to the household of the additional housing that it is forced to consume may be small relative to its costs if the addition permits the household to gain substantial assistance. Conceivably, the household may even rent additional housing which, in itself, does not offer any benefit to the household other than qualifying for assistance.

The detrimental effects on economic efficiency of a minimum quantity of housing constraint are difficult to determine except on a case by case basis. For the households that already do qualify, the allowance is like a pure income transfer and does not affect housing decisions. For other households which do not qualify initially, the constrained housing allowance may be a substantial factor distorting their consumption patterns.

10.0 Administrative Efficiency

10.1 Direct Costs

The administrative structure required for a demand program depends substantially on its characteristics. Kershaw and Williams (1981), in their study of the administrative lessons of the housing experiments, identify four administrative functions: i) outreach, ii) supporting services, iii) inspection and iv) certification. All housing allowances, regardless of design, must incorporate the outreach and certification functions. Outreach is used to identify and inform the eligible population so that they apply for benefits. Certification refers to the determination for eligibility for benefits under the program on the basis of income and family size. Certification is not only required at the time of entry but it is also required to establish continuing eligibility for benefits and also the size of benefits. Supporting services and inspection are required only for programs which either limit benefits to actual expenditures on rental housing or require the household to occupy minimum standard housing. The supportive services are provided to assist applicants in meeting the requirements of the program. Inspection is required only in programs with a minimum housing requirement to ensure that applicants occupy housing that meets the required standard.

The administrative experiments conducted in the United States provide a source of information with respect to the costs of operating a housing allowance program. Table 4.6 presents the median costs of administering the experimental housing allowance program. As can be seen, enrollment costs averaged $253 per recipient and maintenance costs, $205 per year per recipient.

Aaron (1981) provides a different perspective on the administrative costs under the experimental housing programs and its relation to the costs of other assistance programs:

> A freestanding housing allowance program would incur administrative costs estimated at 23 per cent of total program costs. Average administrative costs under existing welfare programs run about 10 per cent of program expenditures. (p. 83)

The reason for this difference, however, should be made clear:

TABLE 4.6

Median Administrative Costs in Eight Administrative Agency Experiment Sites, 1976 dollars

Direct intake costs per recipient		
Outreach	15	
Screening	13	
Certification	8	
Enrollment	14	
Services	13	
Inspection	15	
Total direct intake costs	78	
Total intake costs (including indirect costs)		253
Direct maintenance costs per recipient		
Payment operations	13	
Recertification	16	
Reinspection	7	
Services	34	
Total direct maintenance costs	70	
Total maintenance costs (including indirect costs)		205

SOURCE: Kershaw and Williams (1981), p. 326-27.

> Administrative costs associated with the housing allowance experiments were smaller per case... The explanation for this minor paradox is that payments per case under the housing allowance experiments were much smaller - $64 to $81 per month - than average AFDC payments - $256 a month. (p. 83)

A number of features of this evidence on the costs of housing allowances limit its usefulness for guidance on the cost of administering similar housing allowance programs in Ontario. The administration of the experiments posed problems that could be avoided or more readily overcome in a permanent program. For example, the experimental programs faced higher costs of attracting participants than would be expected for a permanent program. The duration of the experimental programs limited the life-time value to households from qualifying for the program. Moreover, the period over which households could discover the program and learn about the means for qualifying for benefits was strictly limited. A continuing program would have the advantage of a learning period over which households will become familiar with the nature of the program, whether eligible or not. Some households would thus know about the program at the time of any change in circumstances which made them eligible.

The geographical coverage of the experiments also limited the means that could be used for publicizing the program. Each of the experiments was limited to a single urban centre, making many forms of publicity inefficient or impractical. A full fledged program on a provincial basis would have a wider range of media for reaching the target population.

It is clear that housing allowances vary substantially in terms of the administrative apparatus required to implement and administer them. Unconstrained housing allowances require that the eligibility of households for assistance can be established in terms of income and family size. They share these characteristics with many other social assistance programs. The addition of a rent requirement, which bases assistance on actual rent paid, requires further information in terms of rental expenditures by households in order to establish any household's entitlement to assistance. Unlike income, rental expenditures are unlikely to be collected as a matter of course in other social programs. Finally, an allowance program with a minimum physical standard would require an even more elaborate administrative mechanism. In addition to whatever is necessary to establish the eligibility of households, the program would also require specialized staff with the qualifications necessary to inspect the housing occupied by program participants and verify that it meets the standard.

Another thing that needs to be considered is the ability to economize on administrative cost by combining the administration of housing allowances with other progams. The experiments do not supply any information on the economies which could be realized by doing this. The possibilities vary according to the features of the housing allowance program. For example, a program without expenditure or housing constraints could be coordinated with the income tax system. Complete integration, however, is unattractive for several reasons. The nature of the personal income tax system neither facilitates the frequency of payment required for a program of income maintenance nor the ability of the program to respond to changing needs of households. Reliance on the income tax system would also limit the ability of the program to reach those households which do not file income tax returns. This shortcoming is quite serious, for this group comprises a key part of the target group. A program with either an expenditure constraint or a minimum standard for housing would be even more difficult to integrate with the tax system.

As an alternative, the demand program could be integrated with other income support programs such as welfare. The two programs appear to serve clientele which overlap extensively. However, the program may be intended to serve a group such as low-income working families which is beyond those households receiving welfare. In addition, to the extent to which the demand program included housing requirements, some addition would have to be made to the administrative apparatus currently used for welfare.

10.2 Indirect Costs of Administration

Demand programs also differ in terms of the indirect costs imposed on the public through the administrative mechanism. They generally require households to take the necessary steps required to establish and maintain their eligibility for benefits. An unrestricted assistance program does not make any further demands on participants. They have neither to document their housing expenditures nor to demonstrate the quality of the housing that they occupy. The other types of programs do. An expenditure requirement forces households to document their housing expenditures, whereas, a housing standard may require households to document the quality of their housing. Households which occupy substandard housing face higher costs. They must either take steps to have their housing improved or they must search out alternative housing that meets the standard.

10.3 Flexibility

Demand policies permit a wide degree of flexibility to policy makers in adapting to changing needs with respect to adequacy of income. If they decide that a greater level of support is required at an aggregate level, they can adjust the formula on which the allowances are based. Similarly, the changing needs of individual households can be readily taken into account in the formula. The responsiveness of housing allowances' benefits depends on the frequency with which revisions are made to the income and rental expenditures used in calculating benefits. While the same flexibility of policy is available with respect to the housing adequacy goal, individual beneficiaries may be able to adjust to changing housing needs but the policy is only able to affect the size and nature of the housing stock over the long run.

11.0 Community Needs

Demand programs provide a greater opportunity for households to make their own choices about housing than public housing or rental support programs. In these programs, the participants have only the choice of limited locations and as a result are separated from the rest of the community. Housing allowances are, thus, consistent with the goal of encouraging diversity within and between local communities.

12.0 Feasibility

12.1 Level of Government

A demand program could be implemented by either the federal or a provincial government but would face more serious problems at the local level. A major problem with the implementation of housing allowances at the municipal level arises from the mobility of households. On the one hand, households will be attracted toward local governments which offer more generous housing benefits, increasing the costs to local taxpayers from supplying this benefit. On the other hand, housing allowance programs conducted by local governments will reduce the choice of households to those rental units available within the jurisdiction of the local government.

12.2 Cooperation Among Governments

In theory, an unrestricted demand policy can be implemented by either the federal or by provincial governments without the cooperation of other levels of government because the assistance is paid directly to households.

12.3 Political Support

One type of demand policy, the housing allowance, in one form or another, has gained much support from a variety of sources including the Ontario Economic Council, the Canadian

Association of Homebuilders, Dennis and Fish in the report of the Low-Income Housing Task Force and the Canadian Council on Social Development. Yet as discussed earlier, housing allowance programs differ and each form of housing allowance has a different base of support.

The political appeal of an unconstrained housing allowance is probably least among the different forms of housing allowances. Undoubtedly, it would gain support of the target groups because it provides an income transfer which is unconstrained by spending requirements. Such an income transfer, as discussed above, is valued more highly per dollar of cost than a restricted transfer which is, in effect, a transfer in kind.

The other important constituencies for housing policy include developers and landlords. An unrestricted housing allowance offers less appeal to this group because the lack of any constraint means that only a minor portion of the benefits from these programs would end up being spent on rental housing. Any appeal to this group must depend on the indirect benefits it offers. To the extent that an unrestricted housing allowance can reduce concern about affordability through raising incomes of target households, through insulating households from rent gouging and through helping to ensure security of tenure, they may be viewed as reducing the need for rent regulation. Landlords would likely support a substitution of housing allowances for rent review because it shifts the burden of subsidizing affordable housing from them to taxpayers at large. The developers' interest in an unrestricted housing allowance is similar; the demand for construction of new rental housing would likely increase if the introduction of housing allowances permitted reduced reliance on rent regulation.

The final interest group concerned with housing allowances consists of taxpayers in general. The introduction of most demand policies, including housing allowances, would have to be financed from general revenues. Thus, the substitution of housing allowances for rent regulation as the chosen instrument for addressing the affordability objective would consist of a substitution of a program financed by general taxes for a program financed by "taxes" on landlords in the form of a restriction on the rents they are permitted to charge.(10) Despite the equity considerations in such a change, taxpayers are unlikely to be enthusiastic about this additional charge on general revenues.

Political support for demand purposes may also be affected by the controllability of the costs of new programs being considered for implementation. This issue is particularly relevant because the experience with demand policies such as housing allowances in Canada has been very limited. Furthermore, a general wariness can be expected since the introduction of social programs frequently reveals consequences that were unanticipated by policy makers at the planning stages. In particular, programs become more expensive than anticipated because of unexpectedly high participation rates or because the benefits are increased over time. This consideration is especially important for housing allowances as compared to other programs which are based on expenditures from budget allocations. Policy makers set the parameters of a housing allowance program but the actual cost is uncertain in that it depends on unknowns such as the response of the target groups.

13.0 Scale of Costs

Table 4.7 provides a summary of several estimates of the cost of housing allowances for Canada. Those estimates cover such a broad range that they offer little guidance for policy makers.

The first and most widely cited estimate of the cost of a housing allowance is the CMHC (1980) estimate. Apparently, this estimate referred to housing allowance assistance based on a "housing gap" formula of the form:

$$S = a\ (R-bY)$$

> where S is the allowance, "a" is the per cent of the housing gap paid in the form of an allowance, "R" is the program client's rent payment, "b" is the required contribution rate, and "Y" is the client's income. (Falk, 1982, p. 11)

The benefits rate, a, was set at 0.75 and the required contribution rate was 0.3.

Clayton has described CMHC's method in more detail:

> The methodology employed in making this estimate was to examine the current housing expenditure and incomes of Canadian households. For those households whose housing expenditure was less than 30 per cent of current income a subsidy cost of $0 was computed. For households spending in excess of 30 per cent of income on shelter, 75 per cent of the excess was imputed as the subsidy cost. The major assumption employed in using this procedure is that households will not increase housing consumption as a result of the subsidy. (Clayton, 1981, p. 30)

This estimate suggests that a housing allowance of this scope would cost $400 million on a national basis.

TABLE 4.7

Estimated Cost of Housing Allowance Programs

Estimated Cost	Source	Comment
$400 million	CMHC (1980)	Static assumptions
$4 billion	Clayton (1981)	Simulation model to incorporate dynamic response in the market
$211 million (1980) $299 million (1984) $170 million (restricted eligibility)	Steele (1985)	Static assumptions with a 60 percent participation rate
$110 million (1980) with 100 percent participation $77 million (1980) with 70 percent participation	Steele (1985b)	Ontario only
$600 to $700 million	Clayton (1984)	

Steele (1984) makes a useful distinction between static estimates and simulation estimates of the costs of housing allowances. Static estimates are calculated "under the assumption that behaviour in the housing is unaffected by the allowance" (p. 6) whereas simulation estimates are designed "to take into account behavioural response and feedbacks from the rest of the economy" (p. 6).

Clayton (1981) developed the first simulation study of the costs of housing allowance programs to overcome the limitations of CMHC's static estimates. He uses the simulation model to derive alternative estimates of the program costs relative to the bench mark of the CMHC estimates and concludes:

> When the comparison was made it was found that the long run annual cost estimate for the six cities was 10.2 times the cost estimate under the assumption that no program induced housing consumption effects take place. (Clayton, 1981, p. 30)

He attributes the difference to two basic reasons:

> First, average subsidies with the no response assumption are significantly less than the average subsidies after households increase housing consumption in response to the program. Second, participation rates are significantly less with the no response assumption relative to a situation where program induced consumption effects are taken into account. The results of the model indicate that many households with a pre-expenditure to increase ratio of less than 30 per cent increase consumption in order to take advantage of the subsidy. (Clayton, 1981, p. 30)

Clayton recognized that the predictions of the simulation differed substantially from the results of the similar housing experiments in the United States. Comparison of the simulations of the U.S. programs for the Canadian cities with experiment experience in the U.S. shows that the simulation models produce overestimates. Clayton concluded:

> Even if the model estimates are 3 times in excess of actual costs which can be expected, it still suggests that the long run annual costs will be over 3 times in excess of the "no response" cost estimates made by CMHC. (1981, p. 31)

More recently, Clayton (1984) has supplied more moderate estimates of the costs of housing allowances. He states:

> From discussions with knowledgeable officials and researchers, the annual cost for a shelter allowance program based on a payment equal to 75 per cent of the gap between 30 per cent of income and a constrained maximum rent is likely to be $600-$700 million. (p. iv)

The difference between these estimates and his 1981 results seems to be attributable to constraints on eligibility. Unfortunately, few details are provided on the techniques used to derive these later estimates.

Steele (1985b) has presented an alternative estimate for the costs of housing allowance programs which gives a dramatically different perspective on the costs of housing allowances to governments. Her estimates are based on the following assumptions:

- rental gap program with support based on 75 per cent of the gap between actual rent and 30 per cent of income
- maximum (threshold) rent for calculating support
- participation rate of 60 per cent of those eligible
- no behavioural response. (Steele, 1985b, pp. 7-11)

She finds that:

> The total cost for 1980, $211 million, is only about half the CMHC estimate for 1980.... The cost

> rises between 1982 and 1984 but the cost in 1984, at $299 million, is only about half the Clayton estimate for 1984. Furthermore if only families and the elderly were eligible the 1984 costs would be about $170 million, or 4 per cent of the cost of the GIS and Child Tax Credit in 1983. (Steele, 1985b, p. 8)

In another study, Steele (1985a) presents similar estimates for housing allowance programs for Ontario alone using an upper threshold rate of the 33rd percentile rent for Ontario urban areas of 100,000 or more people, and the same assumptions for determination of benefits as in her estimates for Canada. Steele finds the costs for 1980 would have been $110 million assuming 100 per cent participation and just $77 million assuming 70 per cent participation.

The wide range of cost estimates for housing allowances poses a dilemma for the policy maker. Unlike programs such as public housing, the costs of a housing allowance program cannot be constrained by budget allocation. They can only be constrained by changing the dimensions of the program in terms of the percentage of gap made up by the allowance, the share of income paid in rents by participants and the upper threshold to rent.

Although the extreme estimates of Clayton (1981) now seem to have been overestimated by several orders of magnitude, a wide range of estimates remains. The experiments in the United States and evidence from provincial programs have suggested that the response to housing allowances is likely to be limited. Nevertheless, despite the decreasing difference among experts, the remaining range from $600 million to $200 million for Canada-wide program, and proportionately less for an Ontario program (perhaps 30%), still leaves much uncertainty for policy makers.

These cost estimates for housing allowances are difficult to assess in isolation. They do give some indication of the costs of a housing allowance, but, at the same time, they leave unanswered any comparison of the costs with those of alternative ways of achieving the same end. The whole approach of this study has been comparative in that a variety of alternative approaches are under review. A further comparison of the costs of housing allowances will be presented in chapter 7. There, attention will be directed to what is gained for the cost through different approaches.

We have now completed our first review of a generic housing policy using the framework developed in chapter 3. Housing allowances were assessed in the present chapter as representative of rental housing policies which are demand augmenting. We now turn our attention to applying the same evaluation criteria to a second category, supply augmenting policies.

Notes to Chapter 4

(1) A housing allowance of this form provided a benchmark for comparison of the other programs under the demand experiments carried out in the United States (to be described in more detail below).

(2) Conceptually, the most stringent requirement could be considered to occur in a program where government assistance is provided to new housing on the condition that units be set aside for qualifying tenants receiving reduced rent. In this paper, that type of program is treated as supply variant of market augmenting policies, however. See Chapter 5.

(3) The following discussion of the demand experiments is based on Freidman and Weinberg (1982) and Allen, Fitts and Glatt (1981).

(4) Note that the unconstrained allowance was a housing allowance in name only. It can be considered more accurately as a pure income transfer equivalent to a negative income tax. A similar interpretation could be placed on the transfers to households that met the housing requirement prior to enrollment in the experiment.

(5) This discussion of the supply experiment is drawn from Allen, Fitts and Glatt (1981).

(6) The net benefit of housing allowances to recipient households may still be positive even though the housing allowance increases rent levels without any increase in the supply of housing. One element of benefit consists of any transfers received and not spent on housing. In addition, increased expenditure on housing does gain additional housing for the recipients. The elasticity of supply means that the recipients displace other tenants from housing through their improved ability to pay more.

(7) The evidence on the responsiveness of the supply of rental housing to rent levels is discussed in Appendix 1 to Chapter 7.

(8) For the purpose of simplicity, this comparison abstracts from such problems at the number of people in the household and the age of the people in the household.

(9) Other evidence suggests that the elasticity of demand for housing may be even more elastic. See Polinsky and Ellwood (1979) for a discussion of the biases incorporated in studies of the demand for housing.

(10) This concern could be reduced to the degree that the taxpayers believe that the effects of rent controls on the supply of rental housing have caused additional government expenditures in terms of rental assistance,

tax concessions to developers and expenditures on direct supply.

CHAPTER 5: ASSESSMENT OF RENTAL HOUSING POLICIES: SUPPLY POLICIES

1.0 Introduction

All policies that have the proximate effect of altering landlords' incentives to lower their rents, to offer more units for rent at existing levels of rent or some combination of the two can be classed as market augmenting policies which work through supply. The government can supply subsidies to rental housing in a variety of different ways. The simplest and most direct approach to the subsidy of rental housing is the direct payment of subsidy to builders or potential landlords for each rental unit that they make available to tenants. Such a subsidy can occur at the development stage of the rental project in the form of a subsidy of part of the capital expenditures or it can be a continuing payment to a landlord for the supply of specified units to the market. Such subsidies can be regarded as general subsidies if there is no condition attached to the subsidy. Frequently subsidies are conditional in that the subsidy is paid only if the builder or landlord satisfy specified conditions. Among the conditions which have been required to qualify for a subsidy include the level of rent, the type of tenant, or the organizational form through which the housing is supplied.

Less direct approaches to subsidizing rental housing work through the tax system or the provision of credit on favourable terms. A subsidy would arise from taxation whenever the tax treatment of some activity differs from the general treatment of economic activity.(1) Credit subsidies can be achieved through supplying credit at below the market rates for comparable projects or through granting government guarantees to private projects. Each of these different types of supply policies could be examined separately. This strategy is not followed in this study. Rather, several selected policies are evaluated as representatives of the genus. This limited scope is achieved at some costs. No comment can be made about the detailed intricacies of the workings of all the individual policies. On the other hand, the broad determinants of the effects of the different types of policies will be essentially the same.

2.0 The Workings of General Subsidy Programs

The proximate effect of a general subsidy program is to lower the cost of supplying rental housing to potential landlords. While the proximate effect of such programs is clear, the ultimate effects may differ substantially depending on the workings of the housing market. In order to focus upon the factors which determine the impact of subsidies on the quantity of rental housing and level of market rents, the workings of the market for rental housing are analyzed under a variety of assumptions about the demand for and supply of rental housing.

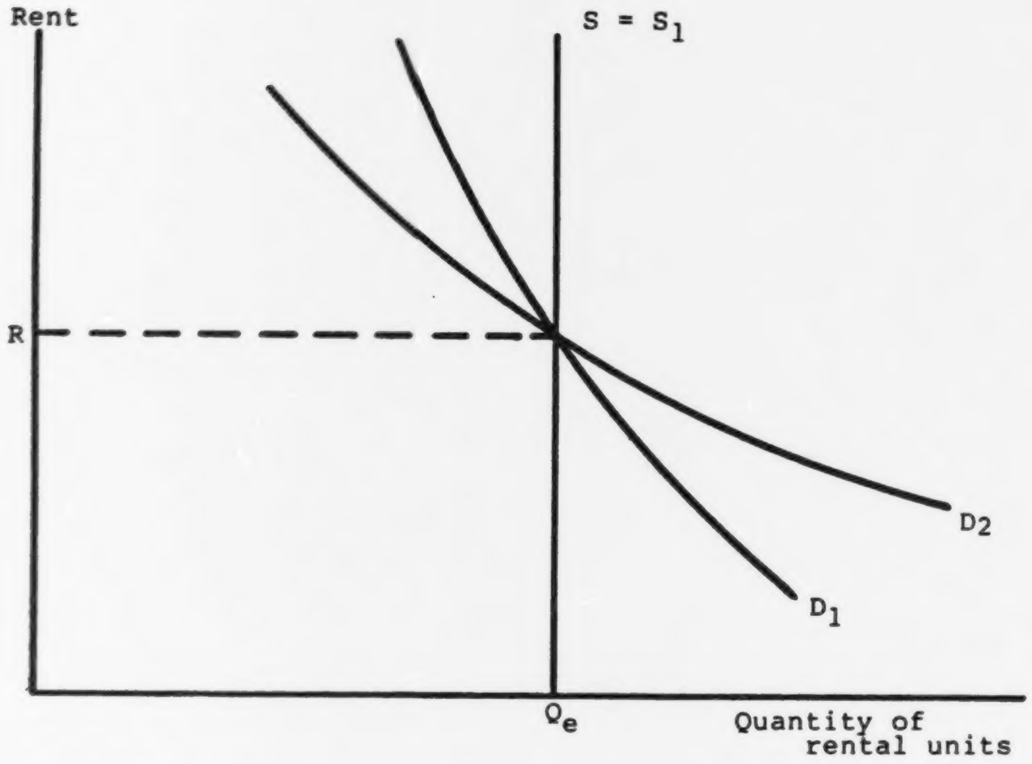
A general subsidy to rental housing works by reducing the costs to landlords of supplying rental housing. While the subsidy can take the form of either a grant to cover the capital costs or a subsidy to meet operating expenses, in either case it can be represented either as capital sum or an annual flow. For present purposes a general subsidy will be treated as a flow in the form of a reduction in the rent needed by landlords to supply a given quantity of rental housing. The analysis will treat the two extreme cases of fixed supply (a supply completely unresponsive to market rent) and perfectly responsive supply in addition to an intermediate case where additional rental housing can be stimulated by higher levels of market rents.(2)

The extreme case of fixed supply is very simple to analyze in that its existence implies that the availability of rental housing is completely independent of the prevailing level of market rents, as shown in Figure 5.1a). The prospect of a subsidy, as a consequence, does nothing to encourage landlords to increase the supply of housing. By the same token, the government should not have to make any expenditures for subsidies on rental housing.(3) A fixed supply of rental housing is unlikely to be descriptive on actual housing markets except in usual circumstances.

A subsidy for rental housing has its greatest impact on the availability of rental units and on the level of market rents when rental housing is completely responsive to the level of market rents. As shown in Figure 5.1b), the subsidy shifts the supply curve for rental housing by the annual value of the subsidy. As can be seen from the comparison of D_1 and D2, figure the effects of the subsidy on market rents are independent of the nature of the demand for housing because the market rent is determined by the horizontal supply curve. In contrast, the effects of the subsidy on the quantity of rental housing depend on the demand curve for housing. As shown in panel b), the subsidy produces a large addition to the stock of rental housing when the demand curve is more responsive to the levels of market rent.

Figure 5.1a)

The Effects of General Subsidies: Fixed Supply



S : supply before subsidy

S_1 : supply after subsidy

D_1 : demand for rental units - unresponsive to rents

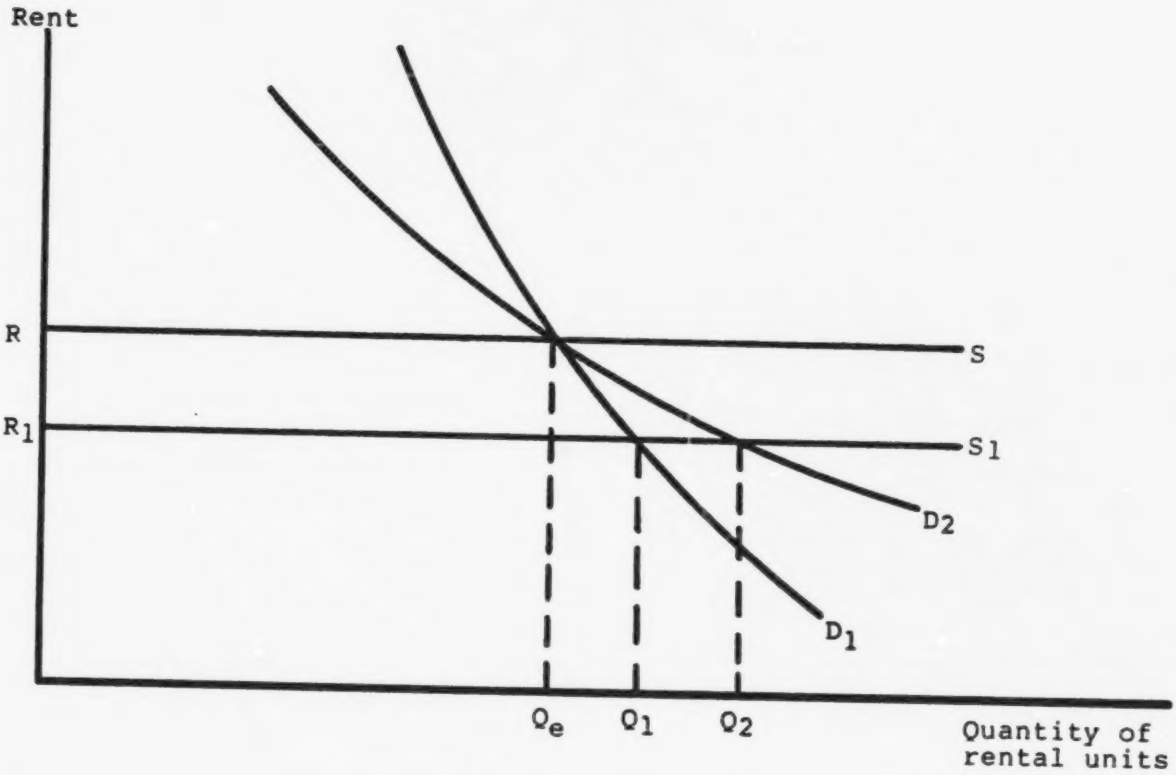
D_2 : demand for rental units - responsive to rents

R : rent before and after subsidy

Q_e : quantity of rental housing supplied

Figure 5.1b)

The Effects of General Subsidies:
Completely Responsive Supply



Rent
R
R_1
S
S_1
D_2
D_1
Q_e
Q_1
Q_2
Quantity of rental units

S : supply before subsidy

S_1 : supply after subsidy

D_1 : demand for rental units - relatively unresponsive to rents

D_2 : demand for rental units - relatively responsive to rents

R : rent before and after subsidy

R_1 : rent after subsidy

Q_e : quantity of rental housing before subsidy

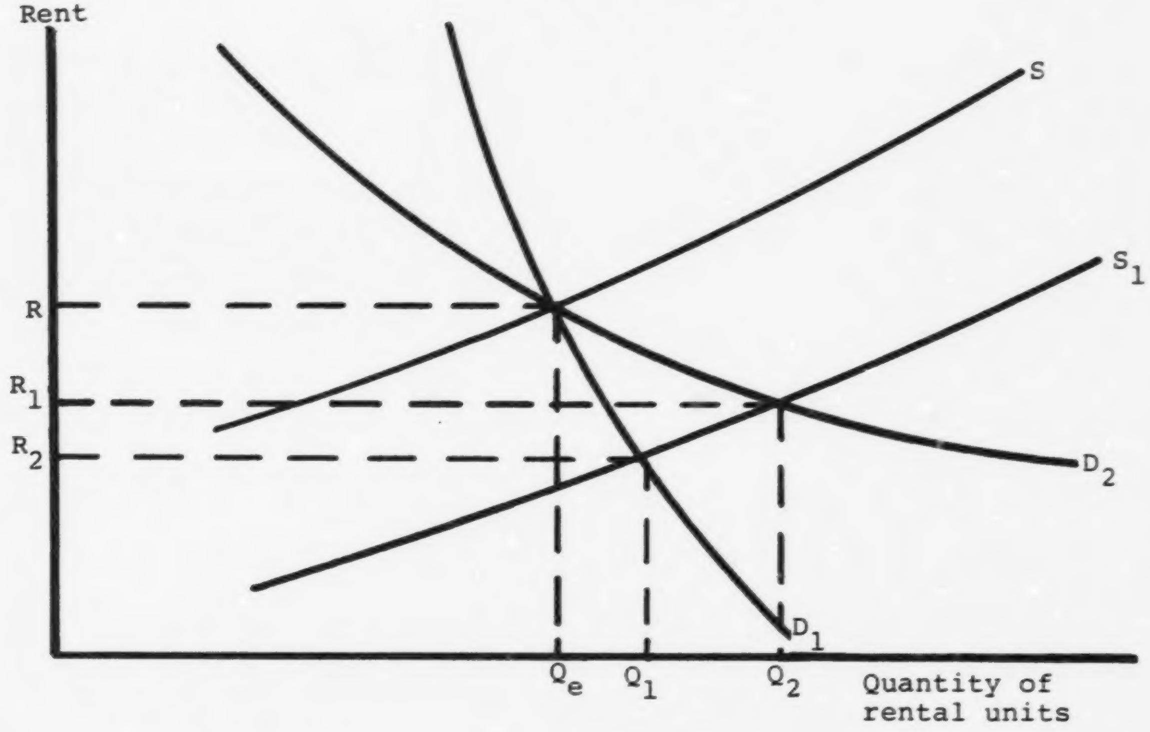
Q_1, Q_2 : quantity of rental housing after subsidy

The rental housing market probably can be best represented by the intermediate case shown in panel c) of Figure 5.1 which lies between the fixed supply in panel a) and the perfectly responsive supply in panel b). The subsidy causes the level of rents to fall and the supply of rental housing to increase, though in neither case by as much as they would with a perfectly responsive supply. Moreover, the ultimate benefits of the subsidy will be distributed differently than in the previous cases. The level of market rents will be lower but less so than with a completely responsive supply and the tenants will not benefit by the full amount of the subsidy. Part of the ultimate benefits would go to landlords because market rents do not fall by the full amount of the subsidy. The distribution of the benefits depends on the nature of the demand for and supply of rental housing. The closer that the supply of rental housing is to the perfectly responsive case, the more the subsidy will go to tenants. Similarly for any given supply curve for housing, more of the benefits will go to tenants as lower rent the less demand for rental housing responds to market rents. On the other hand, the change in the quantity of housing depends directly on the responsiveness of housing demand.

A distinction should be made between the responsiveness of the supply of housing to market rents in the short and long run. The responsiveness of supply in the short run in response to changed rents is limited by the inherent characteristics of rental housing. As Goldberg (1983) points out. "housing is a durable good lasting many decades" (p. 49). Any developer would wish to be assured that the higher level of rents on the benefits from the subsidy is permanent before

Figure 5.1c)

The Effects of General Subsidies: Intermediate Supply



S : supply before subsidy

S_1 : supply after subsidy

D_1 : demand for rental units - unresponsive to rents

D2 : demand for rental units - responsive to rents

R : rent before and after subsidy

R_1 : rent after subsidy

Q_e : quantity of rental housing supplied

Q1, Q2 : quantity of rental housing after subsidy starting to build new units. Once the decisions to construct new units has been made, a long period of time must elapse through planning, approval and construction before the additional rental housing becomes available on the market. Thus the short run supply of rental housing probably responds little to shifts in demand. Most of the pressures are reflected in the level of market rents.

In the long run, the supply of rental housing responds to the presence of subsidies to a greater degree. Many of the rigidities and obstacles to adjustment which are present in the short run disappear or are reduced in significance in the long run. A sufficient time period spans the decision, approval and construction process. Thus the more elastic supply curve for rental housing would appear more relevant to analyzing the ultimate effects of general supply policies.

2.1 Who Benefits?

In measuring the benefits of such a subsidy program, it is important to distinguish between the proximate and ultimate beneficiaries of the housing subsidies. The proximate beneficiaries in these subsidized programs are the developers who receive grants toward the capital costs or landlords who receive annual payments. As shown in Figure 5.1b), the ultimate beneficiaries of these subsidies can be entirely different. The landlords would have been the beneficiaries had the market rents remained at R_0, but the pressure of the increase supply pushed the rents down to R_1, giving the landlord the same return as before the subsidy. The ultimate beneficiaries are instead renters who face lower levels of rent because of the subsidies. It should be noted that because the level of market rents is pushed down by the subsidy, all tenants - not just those living in the subsidized buildings - benefit from the subsidy.

2.2 Cost of Subsidies

The cost of providing the additional rental housing depends on the design of the program and its duration. A blanket subsidy to all suppliers of rental housing, whether existing or new, would be the most expensive form of subsidy. Moreover, only to the extent that it would influence marginal decisions would it affect the housing supply. The benefits to the owners of existing housing would be a pure transfer and would not add anything to the housing stock.(4) An alternative strategy would permanently subsidize suppliers of new rental housing. While the benefits would be identical to a blanket subsidy, its cost would be reduced to the fraction that the additional housing holds to the total stock of rental housing. The costs of this alternative strategy will not remain constant over time. If the demand for rental housing increases, the proportion of the stock of rental housing that receives the subsidy would increase over time. On the other hand, many subsidy programs pay the subsidy in a pattern which provides larger benefits over the early years of a project with declining benefits, and even negative benefits in the later years of the project. Once a program of subsidies has been in place long enough, some of the benefits paid out in earlier years will be recaptured and can contribute to the costs of subsidies on more recently constructed rental buildings.

3.0 General Subsidies: Tax Incentives for Rental Housing

The particular form of program that will be used to illustrate the effects of general subsidies consists of changes in tax policy. Two specific features of the tax system which have been identified as favourable to rental housing are i) the deduction of depreciation for tax purposes in excess of true depreciation and ii) the Multiple Unit Residential Building (MURB) program under which losses incurred in certain rental properties could be used to offset other income for tax purposes. The nature of each of these features of the tax system will be discussed before we turn to an assessment in terms of the criteria developed in Chapter 3.

3.1 Depreciation Allowances

Fallis (1980) argues that one of the most significant tax provisions which favours investment in rental properties is the deduction of depreciation greater than the economic depreciation. These provisions permit a reduction of tax liabilities in the early years of a project when depreciation for tax purposes exceeds economic depreciation. These benefits may be recaptured in later years.(5) Fallis observes:

> The liberal depreciation provisions are not simply equivalent to an extra deduction equal to the difference between allowable and true depreciation, because in the later years of a building's life allowable depreciation will have been used up but true depreciation continues. The depreciation provisions therefore influence the timing of taxable income from a project and the pattern of cash flow. The provisions have the effect of an interest-free loan. (p. 119)

Thus, an excess allowance for depreciation can be considered as a form of accelerated depreciation, though implicit in form.

The importance of this excess provision for depreciation for past investment in rental housing depends on the degree of favourable treatment. On this matter, there is little clear evidence. Fallis suggests that

> In Ontario, it is "generally accepted accounting practice" to depreciate buildings at a rate of 5 per cent for frame buildings and 2 1/2 per cent for other buildings when preparing annual reports. This suggests that the true rate of depreciation might be as little as half the allowable rate. (p. 119)

Frazer (1979) cites a Department of Finance study in 1976 which suggests a true depreciation rate for concrete buildings of 5.6 per cent as compared to an allowable rate of 5 per cent and a true depreciation rate of 7.4 per cent for frame buildings as compared to an allowable rate of 10 per cent at that time. Subsequently, the depreciation schedule has been revised to set the allowable rate at 5 per cent for frame buildings erected after January 1, 1978 (Fulton, 1982, p. 85).

At present, the degree of favourable treatment of capital cost allowances for rental buildings is difficult to determine with any degree of accuracy. The estimate made by Fallis (1980) suggests that allowable depreciation exceeds economic depreciation on "other buildings" but does not on frame buildings. The Department of Finance estimates used by Frazer suggest, if anything, that the rates are roughly equal for concrete buildings but that allowable depreciation falls short of economic depreciation for frame buildings.

The difference between allowable and economic depreciation is not unique to rental buildings. Roger Smith (1979), in his study of tax expenditures, notes:

> According to Corporate Taxation Statistics, capital cost allowances exceeded book depreciation by $3,190 million in 1974 and $3,449 million in 1975. This statistic excludes the non-corporate sector of the economy. (p. 82)

He estimates that addition of the non-corporate sector would add a further $900 million to his estimate for that year. Thus, to some degree, the treatment of accelerated depreciation as special tax treatment for housing is misleading. Rather, the treatment of depreciation of rental buildings can be regarded as part of a more general policy by which:

> Accelerated depreciation is a form of tax expenditure widely used by industrialized and developing countries as a means of stimulating business investment. (Smith, p. 82)

The purpose of the present analysis is not to assess the comparative treatment of rental housing relative to other types of investment in terms of this possible tax expenditure. The relevant issue is the assessment of the use of adjustments to depreciation allowances as a housing policy in terms of the criteria established in Chapter 3.

3.2 MURB's

The Multiple Unit Residential Buildings program has been widely discussed as a tax shelter directed toward encouraging residential investment. The MURB program itself can be best understood as a heritage of the 1971 Canadian tax revision which made the following changes that affected the housing sector:

> - the introduction of a capital gains tax for gains on all financial and real investments except on the sale of a principal residence, with half the gains treated as earned income;
>
> - the creation of a separate depreciation class for each rental building with depreciation being recaptured and treated as income in the event of a sale of a depreciable asset above depreciated value;
>
> - the elimination of the use of real estate as a tax shelter for non-real estate income by prohibiting real estate losses to be used to offset other income, and
>
> - the deemed realization on death of half the difference between depreciated cost and market value on real estate holdings. (Smith, 1977, 25-26)

L.B. Smith (1977) argues that the implications of these revisions were profound for rental housing. Moreover, he suggests that while the introduction of a capital gains tax had a reduced effect because all equity investments were similarly taxed,

> the elimination of the tax shelter and tax on recaptured depreciation was highly significant since it substantially reduced the relative attractiveness of real estate investments compared to other equity investments. (p. 27)

Construction of rental housing decreased substantially after implementation of the 1971 Budget changes. Smith (1977) notes that by 1974 " private multiple dwelling starts had fallen to 56% of their 1969 level while private single dwelling starts had risen by 45%." (p. 27) The MURB program followed a number of measures taken in the May 1974 budget which were directed at encouraging residential construction. They included i) the introduction of the Registered Homeownership Plan ii) the elimination of the tax deduction for the carrying costs of of raw land and iii) the removal of the sales tax on construction equipment. These measures were still judged to be inadequate to provide the desired stimulus to rental housing.(6) The Department of Finance investigated direct programs for housing, especially for low-income households, but concluded that they would be too expensive. The introduction of the MURB program by the Department of Finance reflected a number of considerations on their part:

> The only thing we could come up with that was acceptable...something had to be done that did not cost very much and gave the impression that something was being done for the problem.
>
> You can't do things that are not acceptable so we did the capital cost allowance. Sometimes you have to be seen to be performing things.
>
> Our field people...telling us there weren't many dentists, doctors or lawyers putting money into projects. (Brown, 1982, p. 128)

At the time of its introduction in 1975, the MURB program was believed to be a minor program with a small tax cost. Subsequent experience, as described in section 10 below, shows how wrong this assumption proved to be.

The MURB program constituted a rolling back of the one 1971 tax provision which disallowed the use of any losses from residential rental properties as an offset against other forms of income received by the taxpayer. As a consequence, an investor in an eligible property could apply any "net loss" to shelter other income received by the taxpayer. Goldberg (1983) describes the MURB program as:

> Allowing artificial accounting losses from Multiple Unit Residential Buildings to be used as tax

> shelters, which stimulate the supply of such residential buildings by making them more attractive as investments than they otherwise would be. (p. 65)

Several features of the shelter are particularly significant. Even though the investor supplies only a fraction of the funds for a project and borrows the remainder, the investor as a taxpayer receives the whole of the tax deferral accruing from the losses of the program. In addition, a number of costs incurred in the construction are immediately deductible for tax purposes:

> Such deductions may be permitted either because of some specific provision of the Income Tax Act -such as particular rules that allow taxpayers an immediate deduction for interest, landscaping costs and specified guarantees - or as a result of past practices and rulings of Revenue Canada that allow some administration, guarantee or other charges to be claimed as an immediate deduction when incurred. (Brown, 1982, p. 129).

An incentive exists in these circumstances for investors to rearrange a project to gain the benefits of these so-called "soft" costs. Brown asserts that:

> In the heyday of MURBs, it was not uncommon to find projects in which a third or more of the total costs involved were claimed to be "soft costs", immediately deductible by the investor...(Brown, 1982, p. 129)

Moreover, unlike capital cost allowances, the soft costs were not recapturable so that the recovery in the final sale price was treated as a favoured capital gain for tax purposes.

The experience with the MURB program from 1974 onward would only be partly instructive relative to the implementation of the same measures on a longer term or permanent basis. Brown concludes that because:

> The MURB was initially announced as a short-term program, and then was extended fitfully on a year-to-year basis, investors and developers could never be confident that it would still be in existence when long-term projects were finally brought to fruition. (p. 130)

Table 5.1, from Brown (1982), shows the history of the MURB provision from 1975 to 1982. Thus, for present purposes, the experience of the MURB program must be interpreted in light of the expectation of its temporary duration.

4.0 Assessment of Tax Programs

Two aspects of the taxation of rental housing - the excess of allowable depreciation and the MURB programs - have been discussed as ways in which the supply of rental housing can be stimulated through the tax system. These measures constitute but two of the many possible tax incentives which could be used. For present purposes, the assessment of tax measures as an element of housing policy will rely heavily on these provisions and, most especially, on the experience of the MURB program. As this experience is derived from a program which was announced as short-term and subsequently reintroduced or extended on various occasions, some judgement will be made about the effects of a more permanent program.

4.1 The Workings of Tax Incentives

In order to assess tax incentive programs for rental housing in terms of the present criteria, it is necessary first to examine the manner in which tax incentives are likely to affect the rental housing market. In fact, the effects of such tax incentive programs depend very much on

TABLE 5.1

History of MURB Provisions

	Class 32
Date of Order in Council April 23, 1975	- Class created retroactive to Nov. 18, 1974 for period Nov. 18, 1974 to Dec. 31, 1975
Feb. 4, 1976	- Extended to Dec. 31, 1977
	Class 31
Date of Order of Council April 23, 1975	- Class created retroactive to Nov. 18, 1974 for period Nov. 18, 1974 to Dec. 31, 1975.
Feb. 4, 1976	- Period extended to December 31, 1978
Feb. 9, 1978	- Period extended to December 31, 1978
	- Buildings otherwise in Class 6 for period Jan 1, 1978 to Dec. 31, 1978 added
May 17, 1979	- Period for property otherwise in Class 3 extended to Dec. 31, 1979
	- Period for property otherwise in Class 6 not extended
Oct. 28, 1980	- Proposed that portion that expired Dec. 31, 1979 be reintroduced for period Oct. 28, 1980 to Dec. 31, 1981

SOURCE: Brown (1982), p. 130.

their nature, especially their duration. For present purposes, two extreme cases will be analyzed: a "one-shot" program of limited duration will be compared with a program offering tax incentives on a permanent basis.(7)

A tax incentive offered on a "one-shot" basis applies for only a limited period of time. If, as in the case of the MURB program, some preparatory work must be completed in order for a project to be eligible, only a limited number of rental housing projects would be able to qualify for benefits under the program. Projects which have gained approval under the program will offer to investors, in addition to the revenues of other projects, the tax saving and deferring features provided under the tax incentive program. As a consequence, investors would tend to bid up the price of these projects as long as their rates of return are above those of projects without the tax benefits.

Does this one-shot tax incentive have any permanent effect on the supply of housing? In the most extreme case when the lead time to gain qualification exceeds the duration of the program, it cannot have any long-term effects on the supply of housing. It can only give relief from taxes on projects which are already underway. Even if the duration is sufficiently long to permit some new projects to be initiated, these projects also will be bid up in price to reflect the tax benefits. In the short run, the supply of rental housing is greater than in the absence of the program. After the expiration of the program, new projects will be discouraged temporarily because the projects stimulated by the program place downward pressure on the level of market rents. In effect, the projects encouraged by the tax benefit have been displaced forward in time in order to gain the benefits.

A permanent tax incentive program offers benefits to investors throughout the future as new rental projects are able to offer these tax benefits in addition to the normal returns from such rental projects. Any effect of the program in raising the price of projects gaining the tax benefits will tend to be offset by the initiation of new projects.(8)

Some comparisons can show important differences and similarities between permanent and temporary programs. In both cases, a price difference develops between projects that are eligible for the benefits and those that are not. Moreover, there is no reason to expect the price differential to be different between the two cases.(9) In the "one-shot" case, this price difference results from the bidding up of the few projects eligible for the benefits relative to the much larger stock of existing rental housing. In contrast, in the permanent case, the supply of new projects at a going price sets the price of rental housing and established projects that do not benefit from the tax incentives must be discounted so as to remain competitive for investors.

The price differences which develop in the two programs arise from different sources and should be interpreted accordingly. The "one-shot" policy drives up the price of projects which can qualify for the program. The planning and preliminary work on the project are, in effect, a licence to receive the tax benefits and the resulting price premium created for that licence goes to its owner. In the permanent program, the price of new projects is determined by by land acquisition costs, construction expense and the other expenses required to bring rental housing to the market. The price differential arises because of a discount given to housing which does not receive the tax benefit and is borne by the owners at the time the tax incentive program comes into being.

The programs also have differences with respect to the level of rents and the supply of rental housing. The "one-shot" program produces a transitory increase in the stock of rental housing and a similarly transitory decrease in levels of rent whereas the permanent tax incentive program produces a permanent increase in the stock of rental housing and a permanent decrease in the levels of rent relative to what they would have been in absence of the program.

The two programs have been compared here for a definite purpose. The "one-shot" program captures the off and on, short-term features of the MURB program as it was used as a tax incentive from 1975 to 1981. The above analysis suggests that the use of tax incentives in this one-shot way is unlikely to have any beneficial effects on the rental housing market over the long run.(10) For this reason, the discussion which follows will focus on the effects of a permanent program of tax incentives for rental housing.

The analysis of the effects of permanent tax incentives for rental housing in terms of its effects on market rents and the quantity of rental housing follows the analysis of general subsidies presented in section 2.0 above. It is unlikely to correspond with either of the extreme cases dealt with so far. In reality, the supply of rental housing can be increased over time but with some increase of price. The source of the difference in price is assumed to reflect only long run considerations such as the cost of land and not short run considerations such as those that depend on the level of construction activity.(11) The workings of the housing market without tax incentives is presented as a benchmark for comparison.

4.2 Absence of Tax Incentives

Figure 5.2 shows the market for the purchase and sale of rental housing units in the absence of tax incentives. The demand curve D_0 shows the initial demand by investors for rental housing units in the absence of tax incentives, given population and household incomes. The price of rental housing units is determined by the intersection of D_0 with the long run supply curve. The shape of the long run supply curve reflect the availablity of appropriate housing sites.

Without further evidence, it is not possible to specify the shape of the supply curve of rental housing. It is unlikely to be vertical, or even near vertical, as this extreme would only occur under very stringent conditions: a strictly limited number of sites with a complete restriction on the density with which sites can be developed. The availability of additional sites together with the prospect of fuller development of existing sites increases the ability to add to the rental housing stock with a lesser degree of price increase. Indeed, Appendix 1 to Chapter 7 presents evidence which indicates considerable elasticity in the supply of housing over the long run.

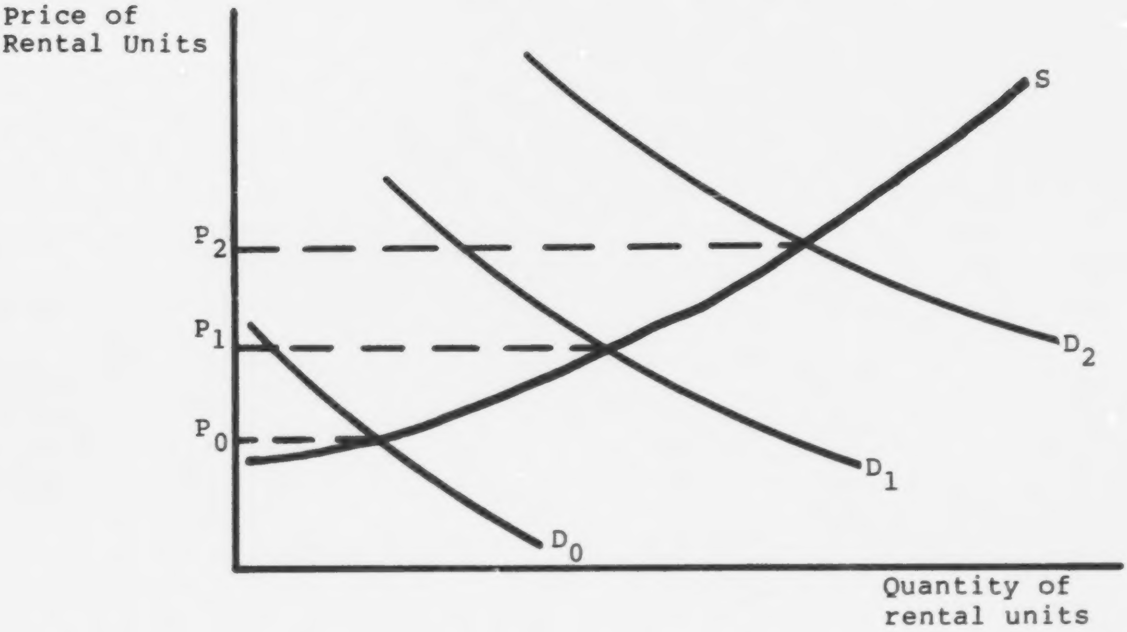
The D curve shifts over time in response to growth in population and income to positions D_1, $D_2 \ldots D_n$. As shown in Figure 5.2b), the price of rental units rises over time with the shift in the demand curve. The increase in the price of rental housing units is an element in the return to owners of existing rental housing and also to owners of sites available for housing. Finally, the fact that rental housing cannot be increased without an increase in the price of rental units means that the level of rents must increase as a result of the pressure of increased population and household incomes.(12) These effects are shown in Figures 5.2c) and 5.2d).

With tax incentives. Figure 5.3 shows the workings of the rental housing market when tax incentives for rental housing are initiated at time t. The demand for rental units increases to the demand curves labelled Dt in each period because, as noted earlier, the return to the investors includes the value of the tax benefits. This increase in demand increases, as shown in Figures 5.3b) and 5.3c), both the price and the quantity of rental housing relative to the values in the absence of the program. As can be seen from Figure 5.3d), the greater supply of rental housing reduces rents below what they would have been without the tax incentives.

The effects of the tax incentive in the case when the supply of rental units can only be increased at a higher price is intermediate between the two extreme cases. The tax incentive both bids up the price of rental units and expands their availability. As in the fixed supply case, some of the benefits go in the form of higher prices to owners of appropriate sites for projects. Unfortunately, the effects cannot be allocated between price and quantity on theoretical grounds alone.

Figure 5.2

a) Market for Rental Units: No Tax Incentives



b) Price of Rental Units: No Tax Incentives

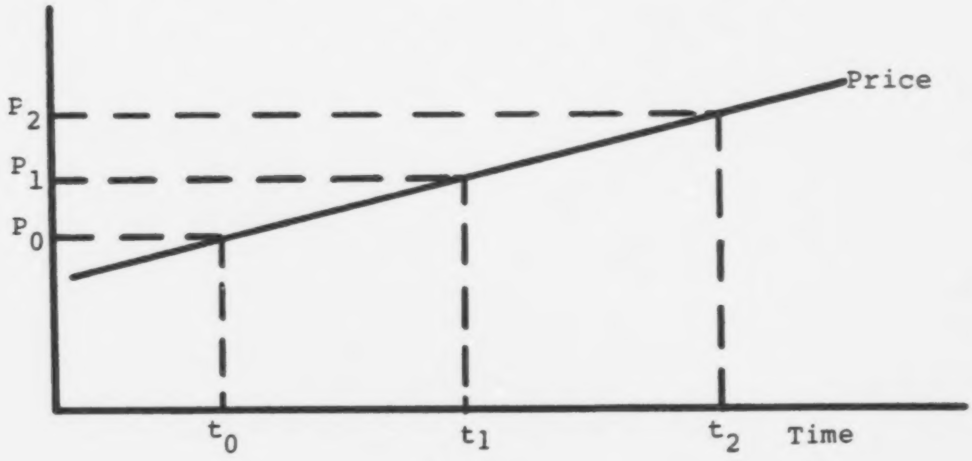
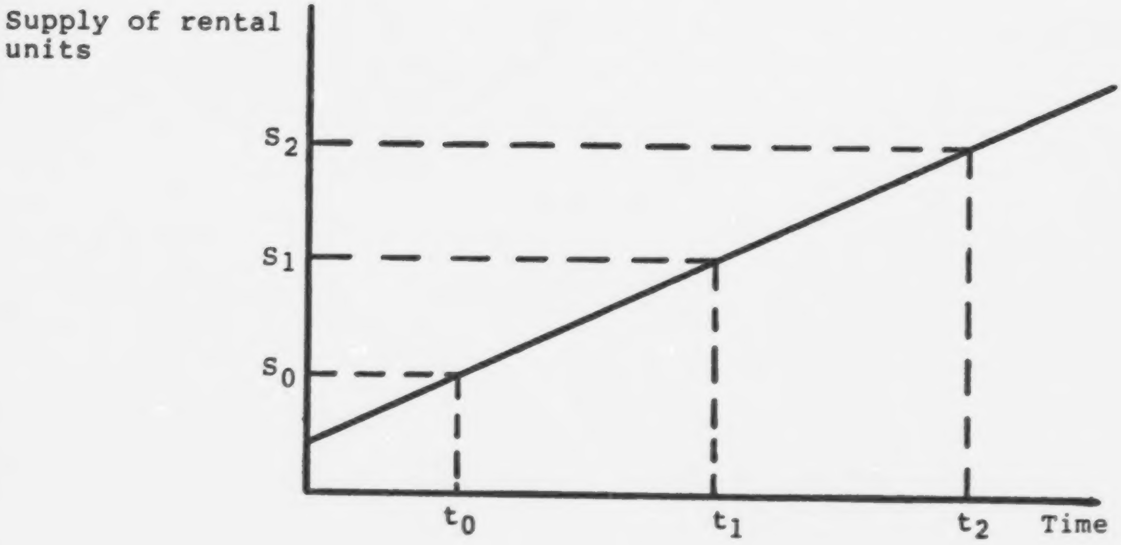


Figure 5.2 (cont'd)

c) Supply of Rental Units



d) Rent levels

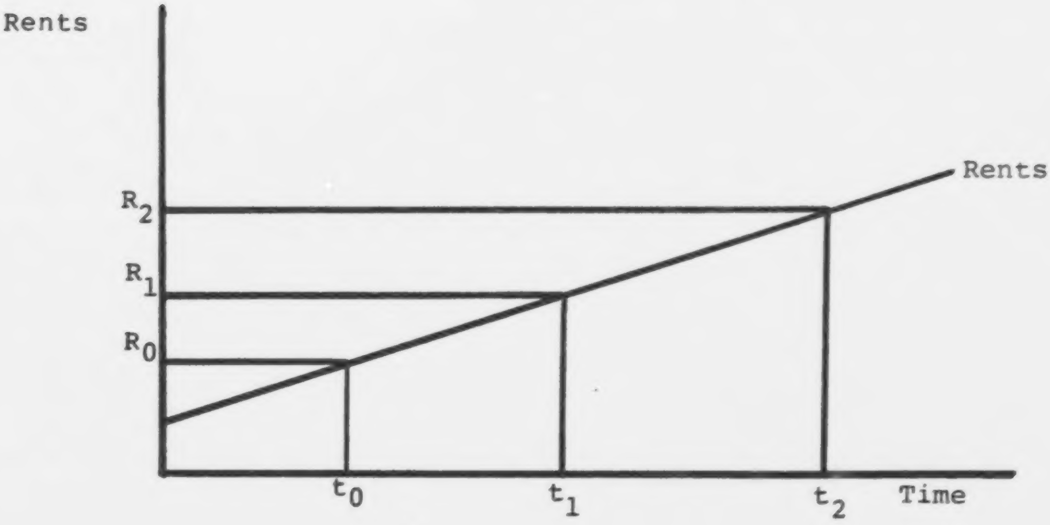
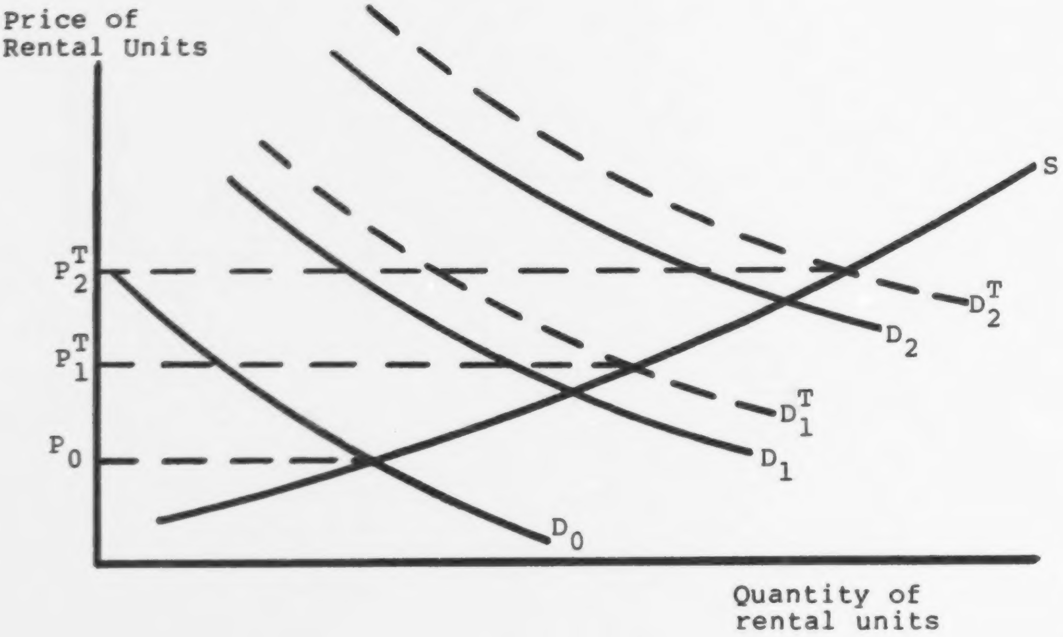


Figure 5.3

a) Market for Rental Housing: Tax Incentives



b) Price of Rental Units: Tax Incentives

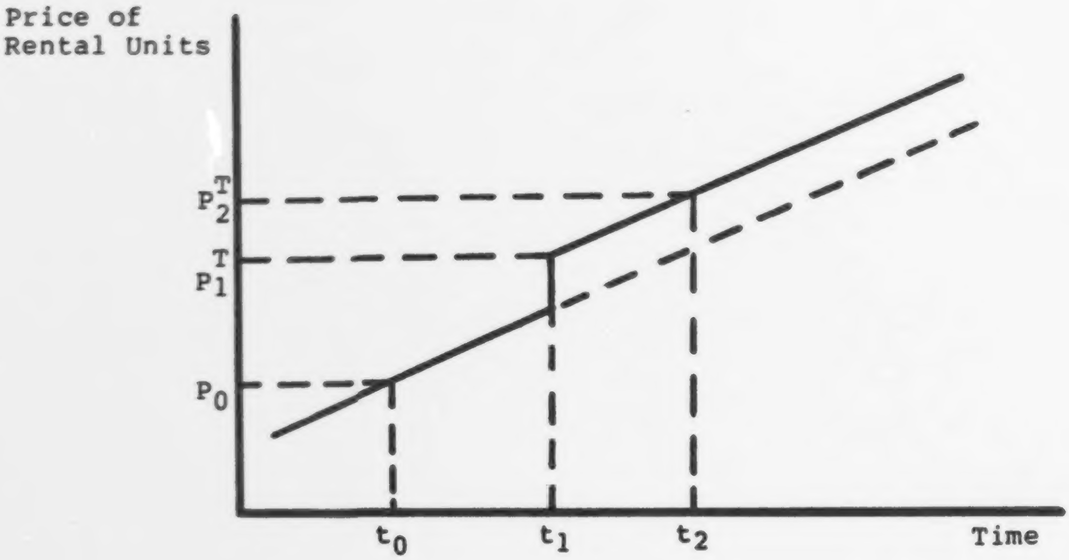
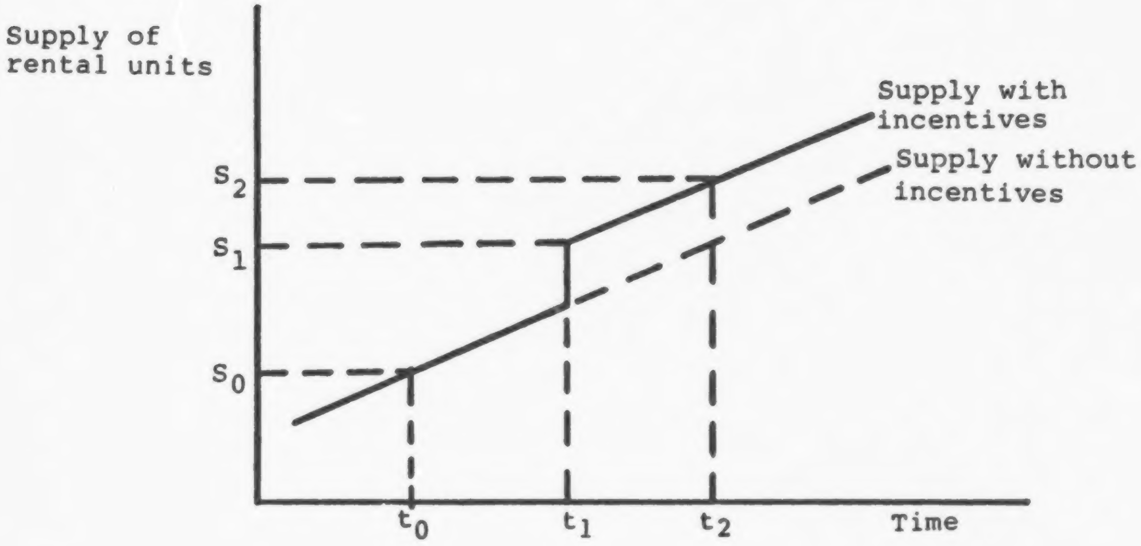
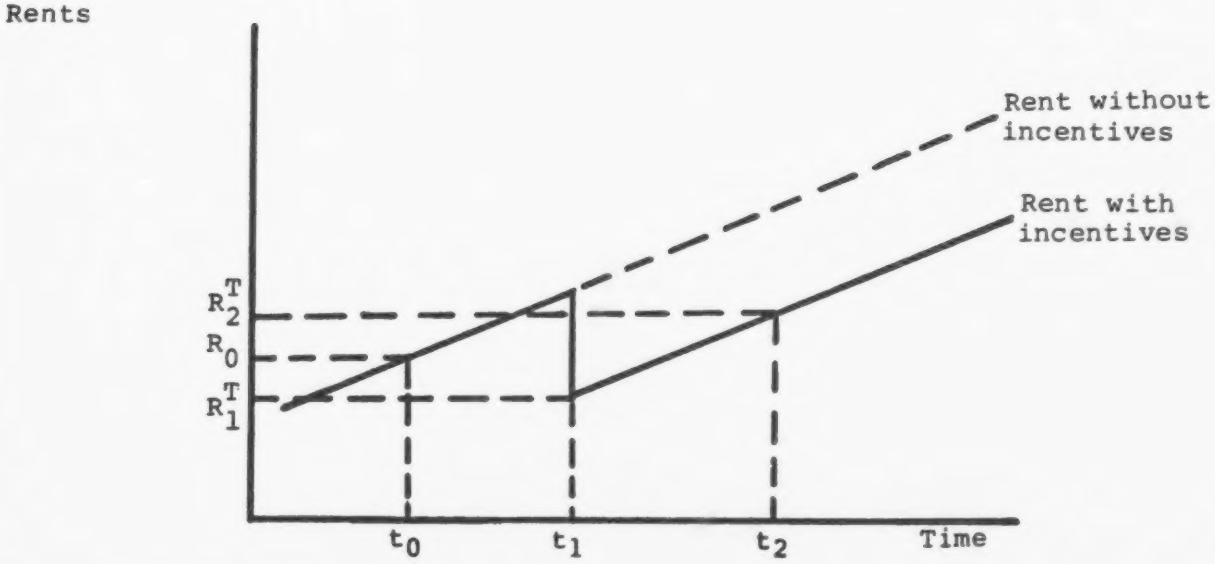


Figure 5.3 (cont'd)

c) Supply of Rental Units


Supply of rental units
Supply with incentives
Supply without incentives
S_2
S_1
S_0
t_0
t_1
t_2
Time

d) Rent levels


Rents
Rent without incentives
Rent with incentives
R_2^T
R_0
R_1^T
t_0
t_1
t_2
Time

5.0 Affordable Housing

Much controversy exists concerning the question of who benefits from MURBs or more generally from the tax incentives directed toward stimulating the supply of rental housing. Part of the problem arises because of a failure to go beyond the proximate benefits of such tax incentives to their ultimate effects. While investors in eligible rental projects are easily identified as the proximate beneficiaries of tax incentive programs, owners of developable sites and renters are also possible beneficiaries of the program. Renters benefit from tax incentive programs to the degree that these programs increase the supply of rental housing. A complete analysis of the effects of tax incentives would require knowledge of the nature of i) the demand for rental properties and ii) the long run supply of rental properties in order to determine the effects of the tax incentive on rent levels and the quantity of rental housing. Existing evidence on the effects of housing programs and on the properties of the housing market does permit the possibilities to be narrowed considerably.

5.1 Adequacy of Income

Fallis (1980) has examined the distribution by income group of benefits from tax allowances for depreciation that exceed economic rates of depreciation. In order to carry out this analysis Fallis needed to make a number of assumptions with respect to i) the financing of the tax benefits and ii) the nature of the long run supply of rental housing. His standard for comparison was an alternative neutral benefit -- neutral in the sense that it would be proportional to income.

He also assumed that the supply of rental housing can be increased indefinitely without any increase in price. In addition, he studied three separate cases using the assumptions shown in Table 5.2 below.

Fallis estimated a range of rent reduction from excess depreciation from a high estimate of 6 per cent to a low estimate of 2 per cent, with a medium estimate of 3 per cent.(13) These estimates are probably on the high side because Fallis did not take any account of effects of the tax benefits on the price of rental housing. Such an effect would have a directly proportional effect on the level of rents. Thus if favourable treatment of depreciation drove the sale price of rental units up by the same percentage as the favourable treatment, the level of market rents would remain unchanged. In calculations by Fallis, there is not any offsetting effect.(14) Even if half the benefit from excess depreciation were reflected in market prices, adjustment of other estimates by Fallis would show that the depreciation benefits reduce the market rents somewhere between 3 per cent and 1 per cent.

The income goal is concerned with the distribution of the benefits of tax incentives as well as their size. Neither the MURB nor the excess depreciation incorporate any provisions that ensure that the benefits are directed at the target groups (i.e., those households that have affordability problems). Frazer (1979) has strongly criticized the MURB program from this perspective:

TABLE 5.2

Assumptions for Analysis of Tax Incentives

	High	Medium	Low
Investor's marginal tax rate	0.5	0.4	0.4
Factor share of capital	0.8	0.5	0.4
Allowable rate of depreciation	0.10	0.075	0.05
True rate of depreciation	0.05	0.035	0.025
Mortgage rate	0.094	0.094	0.094
Life of capital equipment	50	50	50
Adjustment for recapture of tax benefit	0.0	0.1	0.2

SOURCE: Fallis (1980), p. 176.

> The government has a surprising lack of control over the type, location and quantity of MURB projects. Multiple unit residential buildings do not have to meet any detailed design criteria. The federal government's lack of initiative with respect to dictating the form MURB development takes has resulted in units being constructed with an eye to meeting market demand, particularly for "luxury" rental housing. As the demand for housing by low-income taxpayers will not be equated to market demand, it is unlikely that MURB units will ever be suitable for the low-income earner. (Frazer, p. 54)

The first two observations - the lack of both a control mechanism and design criteria - are unobjectionable. Frazer, however, does not supply any evidence with respect to this bias toward "luxury" rental housing. What is clear is that the distribution of the benefits from these programs is determined by the workings of the market for rental housing.

Fallis (1980) has estimated the redistributive effects by household income and age of the excess depreciation allowances as compared to a neutral program which distributes benefits proportionally to income. His estimates, described in Table 5.3, show that:

> If the depreciation provisions were replaced by a neutral alternative, lower-income renters would be made worse off and upper-income renters better off... The result is to be expected because renters spend a decreasing fraction of income on rent as income rises and all enjoy the benefit of a fall in rents, while the neutral alternative assists each household in the same proportion to income....The criterion of vertical equity is also satisfied because the percentage of an income class that benefits falls with income. (Fallis, 1980, p. 123)

Nevertheless, these results do not answer the Frazer (1979) objections entirely. A program may be progressive in its overall effects yet still be vulnerable to the criticism that its benefits are not directed primarily to the target

TABLE 5.3

Distribution by Income Class of Benefits from the Liberal Depreciation Provision, Renters, Ontario 1971

	Average differential benefits($)		
Income ($)	Distribution of renters (%)	Market value measure	Renters as a percentage of the entire class
0 - 1,999	10	-32	48
2,000 - 3,999	11	-26	45
4,000 - 5,999	14	-16	54
6,000 - 7,999	14	- 8	45
8,000 - 9,999	17	2	42
10,000 - 11,999	13	11	35
12,000 - 14,999	11	20	27
15,000 - 24,999	9	40	19
25,000+	1	98	8

SOURCE: Fallis (1980) p. 124.

groups. If the target groups of housing policy from an allocation of income perspective are the lowest income groups in society, then some of the benefits arising from tax incentives for rental housing will accrue to households outside the intended range for benefits.

A most persistent objection to tax incentives programs is that the benefits go to landlords rather than to tenants as the following observers have noted:

Canadian Council on Social Development:

> "Two problems possibly stem from the special incentives extended to landlords and homeowners.... The second is that their effect is generally regressive. The higher the income of the taxpayer, the greater the relative benefit." (1977, p. 62).

Frazer:

> "The capital cost allowance and its companion tax shelter mechanisms are not universally accessible benefits." (1979, p. 45)

Hulchanski (1982):

> "...the tax shelters are of primary benefit to high income investors. In 1976, for example, the Department of Finance (1981) estimated that 66% of all MURB benefits were taken up by individuals earning over $50,000 per year." (1982, p. 10)
>
> "Tax incentives associated with ARP were most attractive to investors with high taxable incomes. Many of the subsidies offered in conjunction with ARP assume the form of tax expenditures directed at high income investors. This fact raises questions about the distribution implications of the program." (p. 28)

Hulchanski (1985):

> "...the Multiple Unit Residential Building scheme designed to encourage the building of new apartments, provided a tax benefit that was really only usable by those in top income brackets." (quoted in Globe and Mail, Jan 12/85, B3)

Hulchanski's concern reflects two separate elements. i) that the tax subsidy programs were directed toward upper income investors and ii) that these investors received excessive tax benefits. The first element, the design of the program to appeal to upper income investors, is not really too surprising. As suggested earlier, the MURB program appears to have been designed to encourage "dentists, doctors and lawyers" among others to finance residential housing projects.

Still Hulchanski's objection with respect to the distributional implications of these programs would be entirely appropriate were the ultimate incidence of the tax benefits identical to the proximate incidence identified in his statements. Yet the proximate effects of the tax incentives is only part of the story. The analysis in section 4.1 has suggested that the benefits of incentives are unlikely to remain with the investor who is the proximate beneficiary as a taxpayer. In one extreme, admittedly an unlikely one, the benefits are captured entirely in the value of eligible sites whereas, in the other more likely extreme, the benefits are passed on through lower levels of market rent resulting from an enhanced supply of housing. In the intermediate cases the benefits are distributed between the value of sites and lower market rents for tenants.

The study by Gau and Wicks (1982) provides support for the position that the ultimate benefit of tax incentives does not remain with the proximate beneficiaries. Gau and Wicks compare the rates of return on a sample of multifamily projects in the Vancouver area with and without MURB benefits. They suggest:

> If investors recognize and respond to the additional cash-flow benefits, they should increase their demand for these properties and bid up the price of the investments. Acquisition prices would rise until r's [rates of return on ARP and MURB investments] equal k [the rate of return expected

> on investments of equivalent risk]. Real estate investors should not be able to earn abnormal or superior returns from the benefits of publically-known, government assistance programs. (p. 7)

Their results provide strong support for their hypothesis:

> These results indicate that real estate investors do not necessarily receive a higher rate of return from the benefits of these two government programs... (p. 9)

This evidence suggests that the redistributive effects of tax incentives should not be judged to flow to the proximate beneficiaries of the programs.

5.2 Adequacy of housing

The other dimension of the affordability objective considers the effects of government policies on the availability of rental housing. As already discussed, this effect is very difficult to determine because of the displacement effect: new rental housing built under any program should not be regarded as net housing because it may displace rental housing which would have been developed in the absence of the program.

Some indication of the effectiveness of tax incentive programs can be determined from making use of our knowledge of the way in which the rental housing market operates. Fallis (1980) has calculated high, low and medium estimates of the effects of excess depreciation allowances on the level of market rents. This information together with estimates of the knowledge of the responsiveness of demand for rental housing to rent levels gives an estimate of the permanent effects of these excess depreciation allowances on the availability of rental housing.

The choice of values for the demand elasticity is crucial for determining the effects of tax incentives on the availability of rental housing. One important source of evidence with respect to housing demand is the result of the demand experiments in the United States. Hanushek and Quigley (1981) report:

> A decade ago, many economists assumed, on the basis of practically no evidence, that the price elasticity of housing demand was above -1.0 or even more elastic. Experimental observation suggests a much lower price sensitivity, at least for lower-income households. In the long run, consumer response to price variation may be somewhat more elastic, but on the basis of this research an elasticity of -1.0 appears much too large numerically. Indeed, unless one believes that the experiment is fatally flawed by its three year time limit, it is impossible to conclude that a 10 percent reduction in housing prices would increase the housing consumption of low-income households by more than 5 or 6 percent. (Downs, p. 204)

In light of these results, the estimates of demand elasticity used ranged from -.7 to -.3, with a medium value of -.5.

Estimates of the effects of tax incentives on the housing stock are presented in Table 5.4 for a variety of assumptions with respect to the effects of the depreciation tax benefit on market rents and with respect to the sensitivity of rental demands to market rents. Given the range of variables used in the estimates, the effects of excess allowance of depreciation could have a permanent effect of from less than one to more than four per cent of the size of the rental housing stock.

More important for present purposes than estimates of the past effects of such programs is the sensitivity of the housing stock to tax incentives. The estimates in Table 5.4 can be used to simulate the effects of any general tax incentive. Fallis used a marginal tax rate of 0.5 for his high estimate and of 0.4 for his other estimates. Thus the high, medium and low estimates represent the effects of a tax incentive with a value of 2.5, 1.6 and 1.0 per cent of the capital component of the housing stock.

The estimates in Table 5.4 indicate that the long run effects of tax incentives on the supply of rental housing. At the middle value for demand elasticity, there appears to be a one-to-one correspondence between the value of the tax benefit and the percentage response in the availability of housing.

One shortcoming of the analysis to this point is the use of the assumption that the rental housing stock can be expanded indefinitely without any change in price. As shown above, the removal of this assumption can change the analysis substantially. For example, if the price of rental housing must increase by one per cent for every one per cent increase in the rental housing stock, the response in the housing stock will be changed from the earlier estimates as shown below in Table 5.5. The significance of these estimates is examined with respect to the effectiveness for cost in Section 6.0 below.

TABLE 5.4

Effects of Tax Benefits from Excess Depreciation on Availability of Rental Housing*

1. Excess of allowable over economic depreciation	2. Rent reduction (%)	3. Demand elasticity	4. Effect on availability of rental housing (%)
.05	6	-.7	4.2
		-.5	3.0
		-.3	1.8
.04	3	-.7	2.1
		-.5	1.5
		-.3	0.9
.025	2	-.7	1.4
		-.5	1.0
		-.3	0.6

* For values of other variables by Fallis, see Table 5.2 above.

SOURCE: Derived from Fallis (1980)

TABLE 5.5

Response of Rental Housing to Tax Incentives: Alternative Supply Assumptions

	Middle range estimates: Rent reduction = 3%	
Demand elasticity	Estimate of supply	Response (%)
	(Es = ∞)*	(Es = 1)**
.7	2.1	1.2
.5	1.5	1.1
.3	0.9	.7

NOTE: Calculated by linear approximations
* Rental housing can be expanded without any change in price.
** A one per cent increase in housing stock requires a one per cent change in price.

SOURCE: Derived from Fallis (1980)

6.0 Effectiveness for Cost

6.1 Adequacy of Income

The effectiveness of tax incentives in terms of affordability and income depends on i) the proportion of the foregone taxes which accrue to the benefits of tenants and ii) the degree to which the benefits of the tax incentives are concentrated on the target income groups. The benefits accruing to tenants from tax incentives in turn depend on the responsiveness of the supply of rental housing to its price. Under the assumption used by Fallis that the supply of housing can respond completely without any increase in price, the tax incentive programs perform extremely well in their ability to redistribute income to tenants. When the supply of rental housing is completely elastic, the entire effect of the tax incentive program in the long run is to increase the supply rental housing and to push down levels of market rent. The entire amount of the taxes foregone by the government accrues to the benefit of tenants, both in and outside the target group.

If the supply of rental housing is not completely responsive to its price, less of the foregone tax revenue goes as a benefit to renters. Table 5.6 shows the effects of different assumptions on the proportion of benefits going to renters. If, for example, the price of rental housing must increase by one per cent to stimulate a one per cent increase in rental housing and the elasticity of demand falls within the expected range, the benefits to renters fall to around one half of the government's loss of revenue. Unfortunately, there is only limited evidence to suggest which assumptions

TABLE 5.6

Determinants of Rental Benefits from Tax Expenditures

Elasticity of supply	Elasticity of Demand	Proportion of foregone tax revenue to renters as benefits
∞	all	100
1	.7	40
1	.5	45
1	.3	65
0	all	0

are most appropriate with respect to the supply of housing. Nevertheless, the evidence that is available, as presented in Appendix 1 to Chapter 7, suggests that the supply of rental housing is quite responsive to price in the long run.

The type of tax incentives used to date in Canada to stimulate rental housing would provide benefits to all groups of renters in the long run. As Frazer (1979) noted, investors choose the types of rental accommodation that will be built in order to qualify for the tax incentives. The tax incentives redistribute income by reducing the general levels of market rents through an increased supply of rental housing. Thus the benefits accrue to all tenants regardless of income. Two factors tend to mitigate the spread of benefits beyond the target groups. As income rises, renters decrease as a proportion of the income group and, in addition, the expenditures on rent decrease as a proportion of income. Nevertheless, a substantial proportion of the benefits accrue to groups other than the lowest income groups in the economy.

6.2 Adequacy of Housing

The effectiveness of tax incentives in increasing the housing stock can be expressed in terms of the number of additional housing units gained as a result of the tax incentives. This effect depends, of course, on the workings of the market and, in particular, on the nature of the demand and supply for rental housing. The use of tax incentives can be an expensive means of increasing the long run supply of housing. Under reasonable assumptions, the cost per unit in terms of lost tax revenue can exceed the value of the housing unit.

7.0 Economic Efficiency

A permanent tax incentive program for rental housing can be expected to have few effects with respect to economic efficiency. Like any other program involving either government expenditures or foregone revenue, some general efficiency cost must be borne in collecting the addition revenue required. The incentive programs could not be expected to alter either the transactions or information costs in the housing market.(15)

The incentive program does preserve the ability of the households that receive benefits to make their own choices with respect to housing. Even in the short run, the tax incentive pushes down rents of all units regardless of whether the units were directly subject to the tax incentive program. All tenants gain the benefits of the program. Thus tenants are not constrained to occupy particular units in order to regain the benefits and can change their housing as their needs change without losing the benefits of the program.

8.0 Administrative Efficiency

The tax incentive programs work through the personal and corporate income tax system. Any additional administrative burden would arise only from the need to certify the eligibility of the project for the tax incentive scheme. Such costs are likely to be minor.

9.0 Feasibility

The tax incentive approach raises a number of problems with respect to its implementation. It either requires cooperation among levels of government or it imposes the costs of a dual system of taxation. Moreover some questions exist about its basis for political support.

The current systems of corporate and personal income tax lead to an effective coordination of the tax policies of the federal government and the provincial government in Ontario in that the two tax systems are administered in common. If Ontario decided to extend the system of tax incentives for rental housing, it would have to persuade the federal government to follow its lead or it would have to forego the benefits of the present, coordinated tax system. The latter alternative would not only increase the costs to the government in the collection of taxes, it would impose greater costs on taxpayers in Ontario in complying with the two sets of tax laws.

One major obstacle to the implementation of further tax incentives arises from the public perception of the incidence of the benefits of the program. Tax incentive programs appear to benefit the higher income individuals and households who receive the proximate benefits from the program. The present appeal of a minimum tax rate for households with incomes above a certain level reflects the same sentiments. Even though these popular views may reflect an incorrect perception of the incidence of the ultimate benefits of tax incentive programs, this perception appears to be sufficiently widely held to limit the prospect of using tax incentives as an instrument of housing policy.

10.0 Cost Estimates of the MURB Program

Earlier in chapter 4, a variety of estimates of the costs of housing allowance programs were presented in order to give some view of the overall magnitude of such programs. These estimates were hypothetical in that they represented the results of simulations of the effects of different policies using estimates with respect to the response in housing markets. In constrast, estimates have been made of the actual costs of the MURB program as implemented in Canada. These estimates are summarized in Table 5.7.(16)

Comparison of these estimates shows a wide difference in costs. Several of the differences are readily understandable. Some estimates include more years than others and include only the costs to the federal government. Others differences depend on the specific assumptions: i) marginal tax costs, ii) the specific taxes allocated, iii) the possibility of recaptured capital consumption allowances on resale, iv) the number of units started under the MURB program and v) the average cost per unit.

The estimates provide a great deal of leeway with respect to the cost of the MURB program. Nevertheless the estimates are more consistent than appearances suggest. The lower estimates are for shorter periods and are limited to the federal government only. Thus the on-again, off-again MURB program appears to have cost the federal and provincial governments approximately $1 billion in lost tax revenues for housing constructed over the period from 1975 to 1982. This

TABLE 5.7

MURB Cost Estimates

Estimated Cost of MURBs for Canada	Source	Comment
$130 million	Department of Finance (1980)	- Includes personal income tax only. Excludes corporate income tax. - No mention of marginal tax rate used nor of number of MURB starts. - Federal revenue losses only.
$392 million	Clayton Research Associates (1981)	- Includes both personal and corporate income tax. - Based on a marginal average tax rate of 36%. - Includes annual tax losses due to deductions of CCA and soft costs. - Excludes resale of MURB from original investor, hence no allowance made for recapture of depreciation or capital gains tax. - Federal revenue losses only. - 75,000 MURB starts estimated for period 1979-1981. - Assume average building costs of $24,000 for 1979, $25,000 for 1980, $26,000 for 1981.
$990 million (1975-1980)	Gau and Wicks (1982)	- Estimates the maximum amount of CCA that could be claimed in years 1976 to 1980. Deductibility of soft costs excluded. - Based on a marginal federal tax rate of 40%. - Assumes 380,000 MURB starts between 1975-1979.
$1,319 million (1976-1982)	Arthur Anderson and Co. (1984)	- Includes deductibility of CCA, soft costs, recapture of CCA and soft costs upon sale. - Projects assumed to be sold in 21st year. - 45% marginal tax rate. - Assumes 195,000 MURB starts between 1974-1984. - Average cost per MURB unit constructed = $63,000. - Includes both provincial and federal revenue losses.

cost can be compared with the initial estimate that the MURB program would be a minor program with a small tax cost.

11.0 Directed Subsidies

Directed supply-side subsidies differ from general subsidies in that developers or landlords are paid to make residential units available to designated tenants. These subsidies can be used either to make existing units available to target households or to encourage the construction of new units under the program. At present in Ontario, the Rent Supplement Programs and the Ontario Community Housing Assistance Program are examples of programs which offer incentives to landlords to provide existing units on a rent-geared-to-income basis whereas the Private Assisted Rental Program stimulates the production of new rental housing for lower income groups.

The programs grouped under the heading vary in many dimensions but show a common characteristic. A subsidy is paid toward the rental of a specified unit of housing. The other dimensions which differ among programs include:

i) payment to landlord or tenants
ii) payment for existing or newly constructed unit
iii) period of assistance
iv) control over rents charged
v) assignment to specified tenants.

12.0 The Workings of Directed Subsidies

Directed subsidy programs differ from general subsidy programs with respect to the criteria used to establish eligibility for a subsidy. In a general program, any project for the supply of new rental housing would be eligible to receive a one-time subsidy of part of its capital costs or a continuing subsidy to cover its operating losses, or some combination of the two. A directed subsidy, for present purposes, is conditional upon allocating some portion of the rental units to specific types of tenants and on favourable terms relative to the market. As is apparent, the distinction between general and directed subsidies is a question of degree as much as of kind.

The MURB program, used here as the prototype of a general subsidy program, is itself a directed program to the extent that only multiple-unit buildings are eligible for the subsidy. For present purposes, attention is focussed upon directed programs which require the allotment of some proportion of rental units to households experiencing affordability problems. Whereas a general subsidy reduces the costs of landlords of supplying a rental unit, a directed subsidy permits a landlord to rent accommodation at below market rents to households with accommodation problems. In effect, directed subsidies of this kind can be treated the same as subsidies to tenants except that these subsidies are tied to particular units of housing.(17) For present purposes, however, directed subsidies are classed as supply policies rather than demand policies.

The analysis of the effects of a directed subsidy on the level of rents and the availability of rental units is quite complicated. The availability of the subsidy to a landlord depends on renting his unit to a tenant who fits the requirements for occupying a subsidized unit. It is not clear how much this tenant would have paid for accommodation in the absence of the subsidy. If the household would have spent as much as the market rent for the unit, then the directed subsidy would alter neither the market level of rents nor the availability of rental housing. While the subsidized landlord gained a new tenant, some other landlord lost one. If the subsidized unit were newly constructed on the prospect of receiving the subsidy, the impact will be to reduce market rents and cause a temporary increase in the supply of housing. In the longer run, the unit built on the basis of this directed subsidy just displaces another unit which would have been built in its absence.

The directed subsidy has a greater effect on market rents if the tenant of the subsidized unit would not have spent as much on rent in the absence of finding the subsidized unit.(18) The subsidy increases the overall demand for rental units in this case. The increase in demand raises market rents and creates an incentive for landlords to increase the supply of rental housing. The final effect depends on the nature of the demand and supply for housing. As in the case of general subsidies, the effect on housing availability will be greater and the effect on rent levels will be smaller the greater the responsiveness of supply with respect to rent levels. In addition, the effects on availability and on rent levels will both be smaller the greater the responsiveness of demand to rent levels.

It could be argued that the distinction between the differences in response by proximate beneficiaries and the overall effect could be approximated by the average response of households so that the analysis would be exactly the same as the general subsidy. This argument would be incorrect because it fails to distinguish between an unconstrained subsidy in the case of the general subsidy and a constrained subsidy in the case of the directed subsidy. Households gain the per unit subsidy under the general subsidy regardless of the quantity of housing that they choose to consume whereas they must consume a specified amount of housing in order to qualify for the directed subsidy. Some households may choose to forfeit the opportunity for subsidy rather than adjust their expenditures in order to qualify. Other households may be willing to adjust their expenditures by more than the equivalent decrease in price in order to qualify for the subsidy.

12.1 Who Benefits?

The distribution of ultimate benefits from a directed subsidy depends on whether the subsidy has any effect on market rents. If it does not, the benefits of the subsidy accrue entirely to the tenants occupying the subsidized units in the form of reduced rent. In this case the in-kind subsidy is valued at close to its market value because the household would have spent exactly the same amount on housing itself. A difference arises when the rental unit does not correspond to the unit the household would have chosen if unconstrained because of differences in location, quality and size.

Other groups of tenants can be affected if the directed subsidy alters market rents because the tenants of the subsidized units change their expenditures. The tenants of subsidized units benefit to the extent of the subsidy less any change in market rents. Landlords of existing units benefit to the extent that the pressure of increased demand pushes up rents. Finally, tenants who do not live in subsidized units suffer because of the higher rents induced by the subsidy. If the subsidies are directed to relatively small groups of tenants, the gain to one group of tenants can be more than offset by the loss to other tenants.

12.2 The Assessment of Directed Subsidies

Directed subsidies, in theory, have the ability to ensure that the subsidies go exclusively toward target income groups. Their shortcomings with respect to income and affordability arise instead from their limited coverage of the eligible groups. CMHC (1979) suggests three sources of low participation:

i) the need to change accommodation
ii) limited awareness of the program
iii) limited supply of units in tight housing markets.

Unlike unrestricted housing allowances, the directed subsidy program requires that in order to receive benefits, households must occupy units which are designated for the subsidy. Under the ARP program, these units were in newly constructed buildings, though this need not be a requirement of such a program. Those households contemplating enrollment in the program must compare the benefits of participation with the costs of changing residence.

The directed subsidy program shares the second obstacle to participation with most other social programs. Many of the target groups appear to be unaware of the qualifications and the necessary steps to be eligible to gain benefits from the program.

The most severe constraint of the directed subsidy program, however, appears to be the dependence of availability of units on market conditions. The program, unlike some others, requires the participation of both target households and suppliers of rental accommodation. Landlords would appear less likely to supply units to the subsidy program when housing markets were tight. As a consequence, a lack of availability of units may restrict the scope of the program when problems of affordability are likely to be greatest.

The effects of directed subsidies on the availability of affordable housing is uncertain. The proximate effect of the subsidy is to remove tenants from other housing into the subsidized units. The fall in demand depends on the amount the tenant would have spent on accommodation in the absence of the program. The overall effect on housing supply depends on the interaction of the reduced demand for other units and the market supply. While a complete displacement seems unlikely, the rental housing supplied under the program is also unlikely to be a complete net addition to the housing stock.

13.0 Effectiveness for Cost

The cost effectiveness of a directed subsidy can be determined with respect to the income dimension of affordability. Directed subsidies are likely to be a cost-effective means of transferring income to target households. The subsidies can be directed accurately to target groups with little spillover to others. The main slippage in cost effectiveness arises because the benefits consist of an in-kind transfer which the households value at less than the equivalent income transfer.

Two possible sources of slippage can be identified with respect to adequacy of housing. First, the effects of directed subsidy may just displace housing which would have occurred in its absence. The cost effectiveness should then be measured in terms of the resulting net addition to the housing stock. This source of ineffectiveness would arise regardless of the design of the program.

A further criticism has been addressed against the actual operation of directed subsidies in Canada. The Assisted Rental Program, the major initiative of the federal government, provided susidized units in newly built buildings. The CMHC (1979) evaluation of ARP declares:

> A further concern is that rent supplements under this program represent a subsidy to 10,500 households, who, except in respect of older limited dividend projects, are mostly consuming the most expensive rental housing in the market place, the newest, and not necessarily the most appropriate. (p. 53)

The directed subsidy offers little protection against rent gouging. The program shares with public housing the need to ration spaces among applicants on a waiting list according to established criteria. The presence of a waiting list means that a victim of rent gouging is not offered any greater protection against above market rents or excessive adjustments than available through ordinary market alternatives.

14.0 Security of Tenure

The effects of directed subsidies on security of tenure are mixed. Assisted households in the program are made more secure in an economic sense. The household is protected against the consequences of any event which either reduces its income or increases the rents it faces for its accommodation. On the other hand, under some programs, the directed subsidies reduce security of tenure in a non economic sense. At a most simple level, directed subsidies require the recipient to occupy specified units made available through the program. They do not permit the recipients to continue to occupy their previous housing. In addition, the program creates additional insecurity because the continuing availability of the units in some programs depends on an agreement between the landlord and the housing authorities. If the landlord chooses not to renew the agreement, the assisted tenant would be faced with either paying the market rent for that unit at the expiration of the agreement or moving to other accommodation.

15.0 Economic Efficiency

The directed subsidy program bears some costs in terms of economic efficiency. Not only must the benefit accrue in the form of housing, the recipient's choice is confined to the housing available through the program. As discussed earlier, the need to take the benefits in the form of housing reduces their value to the recipient, creating an efficiency loss. The restriction to particular units of housing increases the efficiency loss. These units may be unsuitable in terms of location, size and quality relative to the units that the household would have chosen in absence of a constraint.

16.0 Administrative Cost

The direct administrative costs of directed subsidies, in contrast to general subsidies, involve two separate elements. The administrators of the program must procure a supply of housing to offer participating households. In addition, they must select the households that will gain the benefits from the program and determine the benefit to go to each recipient.

17.0 Feasibility

Directed subsidy programs require the cooperation of municipal governments with higher levels of government. The municipal governments are likely to have an advantage in arranging the supply of housing and in processing the applicants for benefits but have very limited sources of revenue. The participation of a more senior level of government would be needed in order to provide adequate funding.

The form of directed subsidy programs as they have been used in Canada encourages the integration of housing. Households which receive assistance are allocated a proportion of the units in a building which otherwise is rented at market rents. This goal appears to have been realized in practice. One limitation arises because of the types of units offered for the assisted rental programs:

> The private rent supplement is of marginal interest to many entrepreneurs and therefore used as a sort of "dumping ground for units". (CMHC, 1979, p. 53)

In addition, while integration appears to have been achieved through the program, it has not avoided the assignment of some stigma to assisted tenants.

> An important aspect of the landlord's relations with the Rent Supplement tenant is the nature of these relations within the context of his relations with other tenants or prospective tenants. One of the major social objectives of the Rent Supplement program is the integration of public housing tenants in privately owned and managed buildings. For all intents and purposes the only persons knowing that rent supplement tenants reside in a building are the landlord, the housing authority and the Rent Supplement tenant.
>
> While this objective looks attractive in theory, in practical terms it does not seem that Rent Supplement tenants can remain anonymous. Through one way or another tenants learn of the existence of Rent Supplements in many instances. As a result of this, 40% of landlords interviewed felt that the reputation of their buildings had suffered because of the presence of Rent Supplement tenants. Most of these landlords were made aware of this through complaints from other tenants. (Raston-Tomany cited by CMHC, 1979, p. 51)

Finally, the political appeal of directed subsidies needs to be considered. The CMHC evaluation observed that:

> In terms of units procured under public housing and rent supplement programs, relative scale alone indicates that rent supplements hardly dented the market. (p. 48)

Despite the introduction of this program coincident with the eclipse of public housing, rent supplement programs did not "take off."

From a recipient's standpoint, rent supplements do provide a benefit but in a more restricted form than through other programs. Similarly private landlords did not appear to be enthusiastic about the program. The program appears to share the disadvantages of public housing. Recipients are unable to avoid the stigma of assistance. In addition, other tenants appear to oppose arrangements for tenants receiving rental assistance in the same building.

This chapter has extended the application of the framework developed in Chapter 3 to policies which affect the rental housing market through augmenting supply. The range of supply policies prohibits any detailed examination on a program by program basis. The analysis examined the effects of both general subsidies such as the MURB program which encouraged rental housing in general and directed subsidies which are intended to support rental housing for low income households. Next the tools developed in Chapter 3 will be used to assess the working of market replacing policies.

Notes to Chapter 5

(1) This definition begs the broader question of the definition of the general treatment of other types of activity. Smith (1977) for example, argues that some of the general tax changes in the early 1970's discriminated against housing relative to other types of economic activity.

(2) This assumption of a fixed supply can be considered an artificial construct. Growth in the number of households together with the supply response to this growth means that demand and supply are continually shifting over time. This construct permits the untangling of the policy effects from other changes which may be influencing the market.

(3) This conclusion would not be valid if the stock of rental housing increased for reasons independent of the level of market rents. Without any way to determine whether new rental units had been stimulated by the housing subsidy, the government would be required to pay the subsidies under the program.

(4) The value of the subsidy transfer can be shown to be identical to the value of the lost revenue from lower rents caused by the increased supply induced by the subsidy.

(5) The proposal in the recent federal budget for a $500,000 capital gain exemption over a life-time, if implemented, would reduce the degree of recapture.

(6) This paragraph on the background to the introduction of the MURB program is based on Brown (1982), p. 128, who, in turn, makes use of David A. Good, The Politics of Anticipation.

(7) This analysis builds on the analysis of general subsidy programs developed in 2.0 above. The extension required because of the "one-shot" nature of the MURB program and the need to compare it with a permanent program.

(8) This analysis assumes that the supply of rental projects can be extended indefinitely at the same cost as existing projects.

(9) A paper by Gau and Wicks (1982) provides evidence that the tax incentive is reflected fully in the difference in the price of rental units according to their eligibility for the tax incentives under the MURB program. Their analysis does not indicate, however, whether the differential arises from a premium on eligible units or a discount on other units relative to the price in absence of the program.

(10) This judgement need not imply that the MURB program was entirely misguided. Its motive may have been the short-

term stimulation of the construction industry, a question beyond the scope of the present investigation.

(11) For a clear exposition of the difference, see Alchian (1977, pp. 273-99).

(12) Note that the higher rents were not described as caused by the higher price for rental units. The higher rents and higher prices for apartments are both the result of a common cause: the interaction of increased demand for housing with a limited ability to increase availability of rental housing.

(13) These estimates are lower than those made by Clayton (1974) in the only other Canadian study. The difference seems to arise because Fallis applied the excess depreciation only to the capital component of the building and considered the impact over the whole life of the program.

(14) These two cases are, of course, the extreme examples developed above.

(15) Smith (1977) does note that MURB program did encourage participation in the rental housing market by investors whose main activity was in other activities. He felt that this would tend to reduce the concentration of ownership. This force would tend to be offset to the degree that these investors must rely on established development firms in order to participate in the rental market.

(16) The sources of difference among these estimates are described in the appendix to this Chapter.

(17) This discussion should serve to emphasise that the ultimate beneficiaries of a policy may be different than the proximate beneficiaries.

(18) It is also possible that the tenant would have spent more in the absence of the opportunity to rent the subsidized unit. Just as the benefits of the subsidy causes some households to increase their expenditures, some households may reduce their consumption of housing in order to qualify for the subsidy. An increase in expenditure seems more likely in that the policy is directed at households with affordability problems.

Appendix to Chapter 5: MURB Cost Estimates

by Pearl Ing

Table 5.7 presented earlier in Section 10.0 provides different estimates of the costs of the MURB program and indicates the principal assumptions on which the estimates are based. The purpose of this appendix is to present in greater detail the methods used for the MURB cost estimates.

In their cost analysis, Clayton Research Associates (1981) use two approaches to look at the cost of MURBs to the federal government.(1) They are:

- The annual tax loss due to the deductions of CCA [Capital Cost Allowance] on all MURBs during a particular year; and
- The discounted value of all of the future CCA deductions on MURBs started (or existing) in a particular year and their implications for tax revenue. (1981, p. 17)

Clayton Research Associates estimated that, at the end of 1980, a total of 170,000 MURB dwelling units were either completed or under construction in Canada. As a result of the reintroduction of the MURB provision in the October 28, 1980 Federal Budget, Clayton estimated 25,000 MURB starts in 1982.(2) Using a marginal tax rate of 36%,(3) the MURB tax expenditure amounts to an estimated $67 million in 1981, up from $49 million in 1978. Table 1 compares the Clayton estimates at selected marginal tax rates with a Department of Finance estimate. Clayton suggests that the Department of Finance (1980) underestimates the federal revenue losses for several reasons. First, Clayton includes an estimate of corporate tax expenditures in their estimate. Second, different assumptions regarding the proportion of CCA comprised by equipment depreciation increase the difference between the two estimates.

The Department of Finance tax expenditure estimates appear to allocate 20 per cent of total tax losses due to CCA claims to equipment and only 80 per cent to buildings. The Clayton estimate allocates 89 per cent of total tax losses due to CCA claims in 1978 to buildings and 11 per cent to CCA claims to equipment.

TABLE 1

Estimated Annual MURB Federal Tax Expenditures, Canada, 1976-1981 ($ Million)

	Department of Finance*	Clayton Research Associates Estimates at Selected Marginal Tax Rates			
		36%	40%	50%	60%
1976	20				
1977	25	n/a	n/a	n/a	n/a
1978	40	49	55	69	82
1979	45	61	68	85	101
1980	n/a	65	72	90	108
1981	n/a	67	74	93	112

* Personal income tax only

SOURCE: Department of Finance, Government of Canada Tax Expenditure Account, December, 1980, p. 22 and estimates by Clayton Research Associates, Tax Expenditures (1981), p. 18.

One interesting point identified by the Department of Finance is that 65.8 per cent of those individuals who reported tax deductions for MURBs had total incomes over $50,000 (1980, p. 19). Arthur Anderson (1984) suggests such individuals would have been subject to marginal tax rates averaging about 64 per cent from 1976 to 1981 (p. 18).

Clayton also provides estimates of the discounted present value of future subsidies required for previously built MURBs, in order to evaluate future costs of MURB projects to the the federal government. Clayton has estimated that all MURB projects started between 1976 and 1981 (estimated at about 195,000 units) accounted for a discounted tax loss of between $560 and $725 million, excluding the complementary effects of soft cost deductibility. With respect to total 1981 MURB starts (25,000 units) only, Clayton estimated that the discounted 1981 value of the federal tax expenditures resulting from the future CCA losses (to the year 2010) on these 1981 starts is between $49 million and $79 million (depending on the discount rate), at an average 36 per cent marginal tax rate. This amounts to the equivalent of a MURB subsidy in the range of $2,000-$3,000 per unit payable as a lump sum grant in 1981 (see Table 2).

TABLE 2

Estimated Discounted Value of MURB Federal Tax Expenditures From Future CCA Losses for 1981, MURB Starts(1) Canada, 1981-2010 ($ Million)

	Discount Rate		
Marginal Tax Rates	10%	15%	20%
36%	79	60	49
40%	88	66	54
50%	110	83	68
100%	132	100	82

NOTE:
(1) MURB starts in 1981 are estimated at 25,000 units.

SOURCE: Estimate by Clayton Research Associates (1981).

Clayton Research Associates (1984) point out that these total tax losses are underestimated since they do not include principal income tax losses, the deductions for other MURB-related tax shelter items such as soft costs and no resale of MURBs from original investors. In addition, the forecast of 1981 MURB starts used in the estimates was lower than the actual number of MURB starts in that year (p. 45).

Taking account of tax losses due to soft cost deductions, Clayton Research Associates estimated that in 1981, the MURB soft cost provisions together accounted for a revenue loss of $134 million, based on a federal marginal tax rate of 36 per cent (the effect of the CCA accelerated depreciation provision is excluded in this total since this would result in double-counting). Table 3 provides estimates of the annual cost of MURBs built between 1976 and 1980. Table 4 presents estimates of the present value of tax expenditures to be incurred in future years as a result of projects started in 1981. Combining MURBs and soft cost deductibility, it is shown that discounted tax losses resulting from 1981 starts range between $140-$180 million, or is equivalent to a lump sum grant of $5,600-$7,200 per unit delivered in 1981.

Gau and Wicks (1982) provide an alternative estimate of the expected level of federal revenue losses from the MURB program. Based on CMHC (1980) data, Gau and Wicks estimate that from 1975 through 1979, there were a total of 578,308 multiple-unit dwelling starts across Canada. Assuming two-thirds of rental units (i.e. approximately 380,000 starts at the end of 1979 were certified as MURBs), and the average construction cost of a new rental unit for each unit (CMHC, 1975: Table 90; CMHC, 1980: Table 100), they present estimates of the maximum amount of capital cost allowances that could be claimed in the years 1976-1980, with an average rate of 7.5 per cent,(4) based on a marginal federal tax rate of 40 per cent. According to Arthur Anderson (1984) and Clayton (1981), approximately 60 per cent of units certified as MURBs were treated as MURBs for tax purposes. This would tend to suggest that Gau and Wicks have overestimated revenue losses.

TABLE 3

Annual Federal Tax Losses Resulting from MURBs, CCA and Soft Costs, 1976-1981

	1976	1977	1978	1979	1980	1981
MURB Provisions(1)	n/a	n/a	49	61	65	67
Use of CCA rather than Actual Depreciation(2)	95	95	95	95	95	95
Deductibility of Soft Costs(1)						
MURBs	n/a	n/a	n/a	54	78	67
Other Private Rental	n/a	n/a	n/a	11	32	49
Total	n/a	n/a	n/a	65	110	116
MURB and Soft Cost Provisions	n/a	n/a	n/a	115	143	134

NOTES:

(1) Assuming a federal marginal tax rate of 36%.

(2) This tax expenditure relates to the total stock of rental dwellings which are being depreciated (not just MURBs).

SOURCE: Clayton Research Associates. 1981, Tax Expenditures - Housing, Ottawa: CMHC, p. v.

TABLE 4

Discounted Federal Tax Losses Resulting From 1981 Rental Starts

Tax Subsidy Program(s)	Discount Period	Interest Rate 10	Interest Rate 15	Interest Rate 20	Direct Spending Equivalent (Lump Sum Capital Grant in 1981)
		($ Million)			
MURB(1)	1981-2010	49	60	79	$2,000-$3,289 per unit
CCA(1)	1981-2010	120	99	83	$2,00 per unit
Soft Cost Deductibility	1981-1986	163	141	127	$2,800 per unit for non-MURBs; $3,200 per unit for MURBs
MURB and Soft Costs	1981-1986	140	141	181	$5,600-$7,250 per unit, or a 15-20% capital grant

NOTES:
(1) Assuming average federal marginal tax rate of 36%.
(2) Assuming average federal marginal tax rate of 40%.
(3) Figures include both personal and corporate deductions.

SOURCE: Dowler, (1983), adapted from Clayton Research Associates. 1981. Tax Expenditures - Housing.

Gau and Wicks' projections indicate that the total federal cost of the MURB program through 1980 is in the range of $670 million. This does not include the cost of the MURB program to the provinces. However, they do provide an estimate of provincial revenue losses:

> In terms of MURB, the provinces with their surcharge tax formula lost the revenue that they would have received given a higher federal tax collection. Based on the foregone federal revenue, the provincial cost of the MURB program through 1980 was around $320 million. (Gau and Wicks, 1982, p. 16, Note 3)

Thus, the combined federal and provincial revenue losses resulting from the MURB program, for the period 1975-1980, is estimated to be in the range of $990 million.

Offsetting this cost in the future will be the federal tax revenue resulting from any recapture of CCA upon sale of the MURB properties. Gau and Wicks explain:

> Since 1972 the Income Tax Act requires that any CCA claimed during an investment which is greater than the actual economic depreciation of the asset be recaptured upon sale and taxed as ordinary income. This "excess" CCA is effectively, an interest-free loan provided by the government during the holding period of the investment. The net cost over time of the incremental CCA claimed under the MURB program is therefore the interest expense to the federal government of this CCA loan. With interest rates for government borrowings at the 15% level and assuming all the incremental CCA will be recaptured, the annual federal interest expense of the above foregone tax revenue is approximately $100 million. (1982, p. 5)

The final total revenue loss estimate which Gau and Wicks end up with is $890 million.

A more recent estimate of government revenue losses resulting from the MURB program has been done by Arthur Anderson (1984). This study examines MURB projects from the viewpoint of an investor. This is a different approach from previous studies since the earlier studies concentrate on the deductibility of CCA to create or increase rental losses. Models were created of four publicly syndicated MURB projects, using the assumptions in the investment prospectuses. Since this approach was designed to evaluate the success of the MURB program in attracting investors, all tax consequences of a MURB project were included. These were:

- deductibility of CCA,
- recapture of CCA upon sale of the project,
- deductibility of "soft costs",
- recapture of "soft costs" upon sale,
- capital gain on sale,
- deductibility of interest on money borrowed to finance the investment,
- deductibility of operating losses and/or income on operating profits. (p. 26)

The following were the key assumptions in this approach:

- The projections in the four MURB prospectuses were assumed to be reliable. Where the prospectus provided only a 10 year projection, the same assumptions were extended for 20 years.
- Projects were assumed to be held by the original investor for 20 years and sold in the 21st year.
- The assumed annual increase in the value of the project over total original cost was estimated to provide the investor with a total net compounded after tax cash return on investment of 10%.
- 45% combined provincial and federal marginal tax rates were used.(5)
- The cost was allocated 2/3 to the federal government and 1/3 to the provinces.
- Approximately 195,000 units were assumed to be MURBs (this is the same number used by Clayton Research Associates (1981)) and are distributed across the years 1974 to 1984 to approximate the year each unit was first claimed for tax purposes.
- An average cost per MURB unit constructed of $63,000 in 1982 was used, projected to other years using the Statistics Canada Residential Building Materials and Wage Rates Index.
- A net present value tax expenditure of 15% of total cost was used in projecting the sample to the total population of MURBs.(6) (pp. 27-32)

Tables 5 and 6 provide summaries of the Arthur Anderson estimates of the current and discounted value of government tax revenue losses resulting from the MURB program. These estimates are higher than the Clayton (1981) estimates since provincial revenue losses are included. On the other hand, recapture of CCA and of "soft costs" upon sale of the project are taken into account. Total revenue losses to both governments resulting from the MURB program for the period 1976-1982 on a current tax expenditure basis is approximately $1,319 million.

TABLE 5

Current Tax Expenditure Summary of the MURB Program
($ Million)

	1976	1977	1978	1979	1980	1981	1982
Provincial Share	33	43	53	63	73	81	90
Federal Share	66	87	108	128	146	165	183
Total	99	130	161	191	219	246	273

SOURCE: Arthur Anderson and Co. 1984. Federal and Provincial Government Expenditures to Assist and Promote Rental Housing in Canada 1976-1982, p. 4.

TABLE 6

MURB Expenditures Summary - Present Value Basis
($ Million)

	1976	1977	1978	1979	1980	1981	1982
Provincial Share	32	38	41	44	48	49	50
Federal Share	66	78	84	84	96	100	101
Total	98	116	125	128	144	149	151

SOURCE: Arthur Anderson (1984), p. 7.

Notes to Appendix

(1) All of the cost estimates for the tax expenditures considered by Clayton Research Associates relate to revenue losses to the federal government only. The provinces also have revenue losses from several of the tax expenditures.

(2) For the period 1975-1980, Clayton estimated total row and apartment starts at 563,145 units. The estimated number for 1981 were 72,000 units. The estimation of the total number of MURB units up to the end of 1980 and projections of 1981 starts were calculated in different ways. The technique for total MURBs up to the end of 1980 involves estimating, first, the number of MURBs in 1978 (based on Department of Finance data), then, updating this estimate to the end of 1980 based on known and perceived market trends. The estimate of the number of MURB starts for 1981 is based on an assumption about the share of total expected row and apartment starts that will be MURBs.

(3) From a sample of 1978 MURB claims by the Department of Finance, Clayton determined that the average marginal tax rate was about 36 per cent of income before allowing for negative CCA income on rental property, but after deductions for soft costs and other tax shelters.

(4) This assumes the starts are equally weighted between Class 31 (5 per cent rate) and Class 32 (10 per cent rate).

(5) Both Arthur Anderson (1984) and Clayton Research Associates (1981) consider a 45% marginal tax rate to be conservative because, according to a Department of Finance (1981) study, average maximum marginal rates were about 64% from 1979 to 1981 and about 50% in 1982 (p.18).

(6) Arthur Anderson regard this discount rate as conservative since the average of the four sample projects was 15.96%.

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CHAPTER 6: ASSESSMENT OF RENTAL HOUSING POLICIES: MARKET REPLACING

1.0 Introduction

Market replacing policies consist of the initiatives taken by various levels of government to intervene directly in the rental housing market to supply housing on a non-profit basis. The market replacing aspects of these policies involve two elements. First, governments may intervene directly rather than attempting to influence the decisions of private decision makers. A primary example is the provision of public housing. In addition, the intervention may also occur on a non-profit basis when the government involved may be prepared to absorb the ongoing losses incurred in operating the project in order to achieve their social objectives.

Market replacing policies can use either of two mechanisms: public housing and non-profit housing. The government itself owns and supplies rental housing in public housing programs. Alternatively it supports private arrangements in the supply of non-profit housing. The reliance on these forms of market replacing policies has changed markedly over the past twenty-five years in Canada. Through the 1960's into the early 1970's, public housing was the preferred instrument used by governments to provide an alternative source of rental housing. Since the early 1970's increasing attention has been directed toward the use of non-profit organizations and co-operatives to replace the market as a supplier of rental housing. In the analysis that follows, attention is directed first toward public housing as a means of replacing the market for the supply of rental housing. Non-profit housing is discussed in the second half of the chapter.

2.0 History of Public Housing

Public housing in Canada, historically, has been conducted through partnerships between the federal and other levels of government. Up to 1978, public housing programs were carried out under Sections 40 and 43/44 of the National Housing Act. Section 40 provided for partnerships of the federal and provincial governments under which capital costs and operating losses were shared between the federal and provincial governments on a 75/25 per cent basis. Section 43/44 authorized the federal government to supply low-interest mortgages of up to 90 per cent of the capital costs and, to grant a subsidy of up to 50 per cent of the losses for low-income housing when tenants paid up to 25 per cent of their incomes on rent. New commitments under these programs ceased in 1978 (Canada, 1985, Appendix 2, pp. 8-9). Since that time, public housing has been supplied under Section 56.1 of the National Housing Act through which provincial and municipal non-profit housing agencies receive assistance:

> Equal to the difference between mortgage amortization cost at market interest rates and at 2 per cent, and is first used to reduce total project cost, including amortization, and operating costs, down to the lower end of market rents. The balance is used to assist low-income tenants residing in the project. (Canada, 1985, Appendix 2, p. 5)

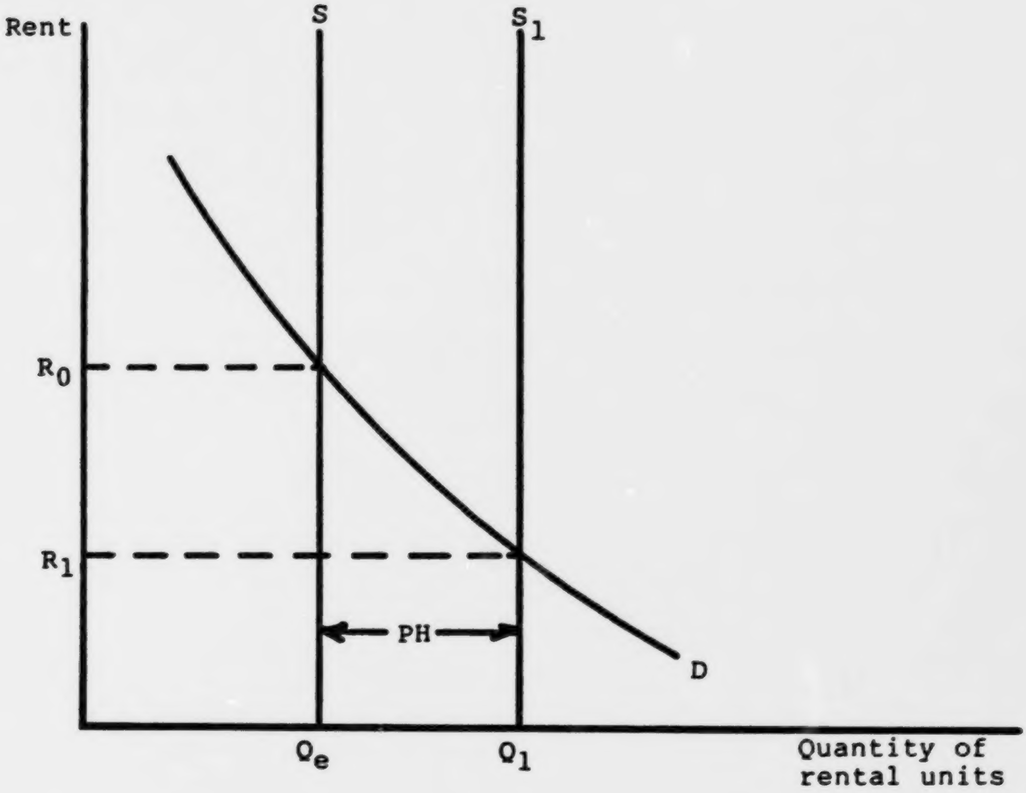
3.0 The Workings of Public Housing Programs

As with other programs, the effects of public housing can be understood best by considering two extreme assumptions with respect to the private supply of rental housing. At one extreme, the supply of rental housing is assumed completely unresponsive to the level of market rents, whereas at the other it is assumed to be completely responsive.

Public housing can be expected to increase the total supply of housing in the case where the supply of housing is totally unresponsive to the level of market rents. As shown in Figure 6.1 the addition of public housing to the stock of housing which already exists depresses the level of market rents, but the lower market rents do not alter the supply of private housing. In the other extreme, the private supply of housing responds fully to the level of market rents. At any rent above the level R, the supply of rental housing grows whereas at any level of rent below R, the supply shrinks. Figure 6.2 shows the determination of the supply of rental housing in such a market prior to the introduction of public housing. Given the demand for rental housing, the quantity of housing would be determined at Q_E, when the demand for rental housing just assures a market rent of R. If a totally unexpected public housing program increased the stock of housing to the quantity Q_p, the level of rents would be driven down temporarily below R to R_a.(1) As a consequence, private suppliers would reduce their quantity of rental housing until market rents are reestablished at R. Without any change in the demand for housing, the quantity of housing will again become Q_E in Figure 6.2 as private landlords

Figure 6.1

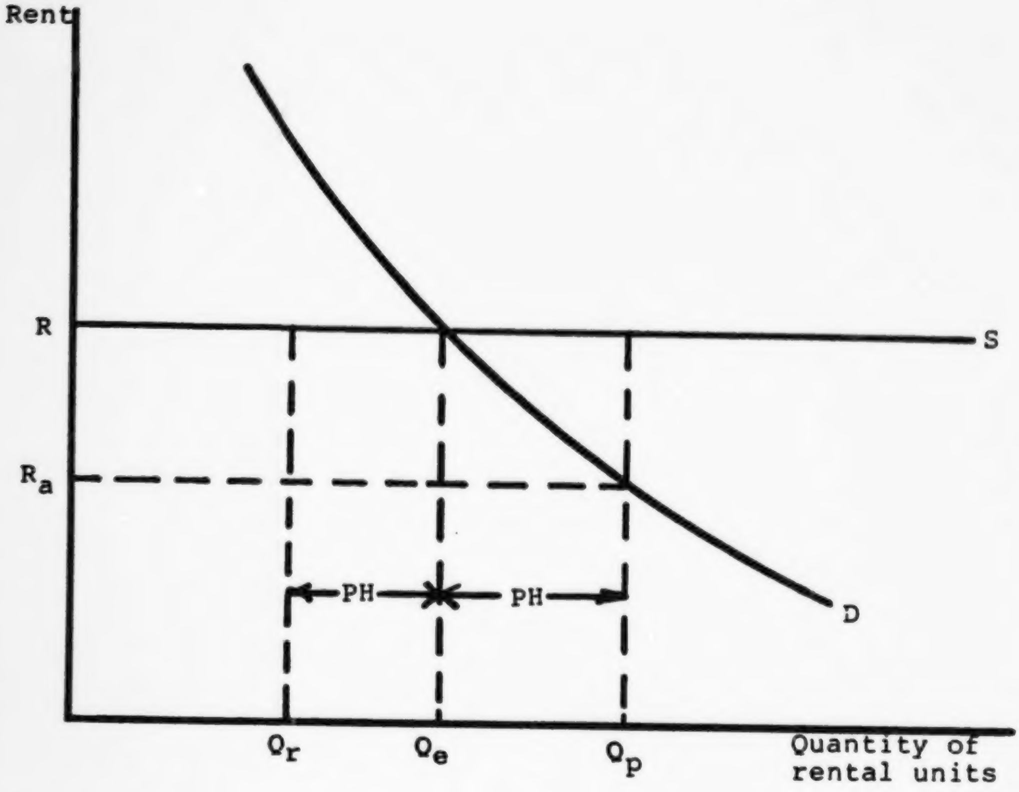
The Market Effects of Public Housing: Inelastic Supply



PH - quantity of public housing
R_0 - rent level prior to public housing
R_1 - rent level with public housing
Q_e - quantity of rental housing prior to public housing; and quantity of privately supplied rental housing with public housing
Q_1 - quantity of rental housing after public housing

Figure 6.2

The Market Effects of Public Housing: Elastic Supply



Rent
R
S
R_a
PH
PH
D
Q_r
Q_e
Q_p
Quantity of rental units

PH - quantity of public housing
R - rent level prior to public housing
R - rent level after adjustment to public housing
R_a - initial rent after unexpected supply of public housing
Qr - private supply of rental housing after adjustment to public housing
Q_e - total supply of rental housing after adjustment to public housing

reduce their supply in response to the lower level of market rents. Public housing in these circumstances has displaced on a one-for-one basis rental housing which would have been available from private suppliers.

The fact that public housing which has been fully anticipated by private suppliers does not have any effects under the circumstances provides another example of the fact that public policy may have unintended effects which tend to offset its original purpose. In the case of public housing, the effect is quite subtle. The new housing produced by the program is visible and easy to attribute to the program. The discouraged supply from private suppliers is less easy to discern and would tend not to be identified as an effect of the program.

One irony of this displacement effect should be noted. To the extent that housing markets are segmented, the displaced housing would more likely be at the lower end of the market. Thus the public housing displaces privately supplied housing which would serve the same needs toward which the public housing is directed.

The effects of public housing on the level of rents and the supply of rental housing are clearly more favourable when the supply of rental housing does not respond to rent levels. The lack of any response to rent levels "short circuits" the displacement effect on the private supply of rental housing. The extreme case of a supply of rental housing which is totally unresponsible to market rent would be unlikely to be present in any housing market over the long run. Private suppliers treat housing as an investment competitive with other forms of investment according to their respective rates of return. Inasmuch as rent levels are an important determinant of the return from housing, the stock of rental housing is likely to be sensitive to rent levels in the long run.(2)

It may be objected that the extreme form of unresponsive supply may be descriptive of the rental housing market in the short run. Even this reservation overstates the likely short-run effects of public housing. The supply of public housing must be a net increase to the supply of housing for this analysis to apply. Yet the planning and construction of new public housing will serve to shape the expectations held by suppliers of private housing units of the rents that they are likely to receive. Thus even in the short run, public housing can displace private rental housing which would have been built in its absence. Public housing is more likely to depress market rents in a housing market in which little growth could be anticipated in the supply of private housing than in one where rapid growth was expected.

4.0 Affordable Housing

4.1 Adequacy of Income

Public housing alleviates the affordability problem by providing rental accommodation to the tenants of rental housing at rents which are below the market level. Analysts of housing policy praise public housing as an instrument of income redistribution. The Canadian Council for Social Development (1977) in its review of social housing policy asserted:

> Criticisms levelled against public housing over the years are legion, but one fact stands out. Whatever else could be said, public housing has served and continues to serve the most-needy Canadians with low-rent housing based on their ability to pay. (p. 69)

Similarly, Marks (1984b) observed:

> Public housing, which is a form of geared-to-income housing, has traditionally been viewed as the most effective and direct means of addressing the affordability problem. (p. 76)

Despite these strong expressions of support for public housing as a measure of income support, the ways in which it achieves these objectives should be examined carefully for present purposes.

An important aspect of affordability entails the ability of a policy to direct resources to target income groups. Public housing achieves this end by setting rents for tenants on the basis of their income, typically no more than 25 per cent. The levels of subsidies achieved by public housing in Ontario during 1983 are reported in Table 6.1.

The beneficiaries of the subsidy inherent in public housing will be determined by the composition of the tenants accommodated at any time. Fallis (1980) has estimated the income redistribution effects of public housing compared to the benchmark of a neutral program of redistribution. The resulting estimates, presented in Table 6.2 lead Fallis to conclude that:

> If public housing were replaced by a neutral alternative, the lower income tenants would be made worse off and higher-income tenants better off using the market value measure of benefits. (p. 60)

TABLE 6.1

Average Monthly Geared-to-Income Subsidies, 1983

	$/Unit/Month	$Rentable Room/Month
OHC[a] Metro Toronto	295	66
OHC[a] Province (excl. Metro Toronto)	207	50
Senior Citizens	179	52
Families	261	48
OHC[a] project total	238	56
MTHCL[b] (senior citizens)	134	49
Commercial rent supplement	225	57
Community-sponsored rent supplement	253	---[c]

NOTES:

[a] OHC: Ontario Housing Corporation

[b] MTHCL: Metropolitan Toronto Housing Company Ltd.

[c] Subsidy per Rentable Room cannot be calculated for Community Sponsored (non-profit) rent supplement units because geared-to-income assistance is not tied to particular units.

SOURCE: Marks (1984), p. 77, from Ontario Ministry of Municipal Affairs and Housing, 1983, Table 42, p. 68; OHC 1983 budget and additional staff calculations.

TABLE 6.2

Distribution by Income Class of Benefits Among Participating Tenants in Public Housing, Ontario 1970

	Average differential benefits($)		
Income ($)	Distribution of participants (%)	Market value measure	Participants percentage of the entire class
0 - 1,999	24	-520	2.1
2,000 - 3,999	25	-172	3.1
4,000 - 5,999	46	270	5.4
6,000 - 7,999	5	696	0.5
8,000 +	---	---	---

SOURCE: Fallis (1980), p. 67

Moreover, as Table 6.2 indicates, in terms of vertical equity, the entire benefit of the subsidy element of public housing was confined to tenants with incomes below $8000 and no more than 5 per cent to tenants with incomes above $6000. This evidence suggests strongly that public housing programs are effective at directing their benefits to the target group of low-income households.

The estimates on vertical equity discussed above most likely overstate the ability of public housing to direct its benefits to target households. Undoubtedly some households misrepresent their incomes in order to qualify for or remain eligible for public housing. Some households may remain in public housing even though their incomes rise above the limits unless they are regularly monitored by the housing authority. Finally, some households may turn down opportunities for better jobs or even for employment itself if acceptance would have jeopardized their eligibility for continuing assistance. Such behaviour would be most likely when the employment opportunity cannot be judged to be permanent. This latter problem is more likely to be a problem for public housing than for other housing programs such as housing allowances. Once a household loses the benefits of public housing, it would have to work its way through the waiting list to regain them.

The other dimension of the affordability goal concerns the degree of horizontal equity attained by various programs. Horizontal equity as applied to public housing refers to the proportion of eligible households receiving benefits under the program. If the proportion of the target groups gaining assistance through public housing is large, then the program can be said to achieve a substantial measure of horizontal equity.

Fallis (1980) presents evidence with respect to the horizontal equity of public housing programs in the form of the proportion of any income class which participates in the benefits from public housing. He finds participation rates of the following magnitude:

Income	Participation rate of income group in public housing
	(%)
0-1999	2.1
2000-3999	3.1
4000-5999	5.4
6000-7999	.5
8000 +	--

The highest participation rate for public housing is little more than one in twenty and does not occur in the lowest income group. The participation rate for the lowest income groups is approximately one in fifty for the very lowest group and one in thirty-three for the next lowest group.

The low participation rates in public housing appear to be widely recognized. The Canadian Council on Social Development (1977) observes with respect to public housing in Canada as a whole:

> Since the traditionally-preferred mechanism over the last quarter of a century has managed to deliver assistance to about 140,000 households who would otherwise be in the same category, it can be assumed that about 14 per cent of the problem has been met. Even if such programs were to be as active as in the past decade, it would take at least another 50 to 70 years to deal with the rest of the problem. (p. 74)

The problem of horizontal equity under the program at present gains further emphasis by the presence of waiting lists for accommodation in public housing. The Association of Municipalities of Ontario (AMO) has assembled data which are presented in Table 6.3 on the number of households on waiting lists for public housing supplied by various authorities in Ontario. These numbers appear to be substantial. A more complete perspective can be seen from the annual experience of one housing agency. Cityhome, the public housing agency of the City of Toronto, reports a waiting list of 4,205 households, with 1,569 new applications received during 1982. The waiting list can be compared with Cityhome's total stock of 3,820 housing units at the time. As can be seen from Table 6.4, the waiting list also appears to be concentrated in the lowest income ranges.

Fallis (1980) presents the criteria used for admission to public housing as shown in Table 6.5. Some further indication of the severity of the rationing problem is revealed by the fact that applicants gain additional points according to the period they have spent waiting to date. Amazingly, the applicant gains 10 additional points for a six year wait. This observation, in itself, indicates the very limited availability of public housing relative to the size of the eligible target group. It is also interesting to compare the allocation of public housing to the non-market rationing system used in the U.S.S.R. which was described in Chapter 1.

The limitations of housing allowances with respect to horizontal equity appear to be exacerbated by the practical administration of public housing. The AMO (1981a) condemns the point rating system as follows:

TABLE 6.3

Selected Waiting Lists for Assisted Housing

		1980	1981
Metropolitan Toronto Housing Authority (OHC)	Families	3,295	4,710
	Seniors	576	608
		3,871	5,318
City Home (City of Toronto NPHC)		2,731	3,569
City of London Housing Authority (OHC)	Families	88	84
	Seniors	90	179
		178	263
Sudbury Housing Authority (OHC)	Families	319	434
	Seniors	74	183
		393	617
City of Ottawa Housing Authority (OHC)	Families	553	874
	Seniors	422	329
		975	1,203

SOURCE: Association of Ontario Municipalities (1982).

TABLE 6.4

Cityhome RGI Waiting List: Annual Household Incomes, December 31, 1982

Income Range	Households Number	 Percent
$0 - 4,999	1,170	32.24
$5,000 - 9,999	1,408	38.79
$10,000 - 14,999	704	19.39
$15,000 - 19,999	260	7.16
$20,000 - 24,999	60	1.65
$25,000 - 29,999	17	0.46
$30,000 - and over	10	0.25
Total	3,629	100.00

Average = $8,143

Median = $6,804

NOTE: Income of 569 households not reported, generally representing social assistance or other fixed incomes to be confirmed when housed.

SOURCE: City of Toronto Housing Department, 1983, p. 38.

TABLE 6.5

Admission Criteria for Public Housing

The criteria used to admit households to family public housing are reflected in the point rating reproduced below, obtained from the Tenant Placement Branch of the Ministry of Housing in Ontario.

The applicant's present situation is assessed and the degree of need is established by a personal interview conducted by a staff member once the application has been processed.

The conditions of need to apply for housing and the categories for points are as follows:

Residential qualifications
Points are awarded for the length of time the applicant has been a resident of Metropolitan Toronto up to ten years (0-10 points).

Overcrowding
It may be assumed that two persons to a bedroom, i.e., husband and wife, or two children of the same sex over five years of age, is the norm. When an applicant who is a householder has caused overcrowding by taking in lodgers, it is not reasonable to award overcrowding points (5 points).

In cases of gross overcrowding where the family is two or more bedrooms short, 15 points are awarded as a health factor.

Separated families
A family not all living under the same roof may be separated for several reasons. Points should be allotted when members of a family are required to live apart because of lack of suitable accommodation: children under temporary Children's Aid; husband is obliged to live away from family because his work is too far from present home; or accommodation is too small (15 points).

Health or Medical Factors
It is desirable to give some consideration to applicants who need to be housed for medical reasons. A doctor's letter is required. It is reasonable to distinguish between illnesses that are affected by housing conditions and illnesses that may be distressing but are unrelated to housing (15 points).

Number of dependants
This is self-explanatory. Points are given for the number of dependent children who are living with the applicant until such time as these children either commence work and leave school or home (0-10 points).

Percentage of income to rent
This should include day care or nursery school costs as part of the total rent cost for working one parent families. A statement from the school is submitted in all cases: 0-25%, 0 pts; 26-9%, 3 pts; 30-4%, 5 pts; 35-9%, 10 pts, 40-9%, 15 pts; 50 and over, 20 pts.

Table 6.5 (cont'd)

Abnormal financial commitments
Some families incur an excessive burden of debt through circumstances largely beyond their control. Prolonged illnesses, specialized medical care resulting from accidents, legal claims, etc. can be contributory factors (15 points).

Waiting period - without offer
People with reasonable needs can frequently be passed in the selection process by the continuing reception of new applicants with higher points. This is recognized by the awarding of points in this category. Where an applicant has been offered suitable accommodation and has refused for personal reasons, the points for waiting shall count from the date of such refusal, not from the date of application: one year, 1; two years, 2; three years, 4; four years, 6; five years, 8; six years, 10.

Structural conditions
A specific number of points can be awarded for any or every facility that is shared or in poor structural condition - includes overcrowding category (0-30 points).

Notice-to-vacate
If the applicant has a notice-to-vacate, the premises then cease to be a factor. Points are given for either poor structural condition or a notice-to-vacate, not both (30 points).

Maximum points 125.

SOURCE: Fallis (1980), p. 167.

> The system employed currently in most municipalities in Ontario seriously underrates the problems of affordability. The present system was designed at a time when the major housing problems were related to housing conditions and, therefore, most of the points are accorded for inadequate housing. Furthermore, there is an inconsistency between the systems in use for families and seniors, in that the system for seniors allocates points for income levels as well as for the rent-to-income ratio, whereas the system for families allocates points only for the latter. The system generally in use for families has a maximum of 125 points. There are no points for level of income and only a maximum of 20 points for affordability problems. Consequently, a household experiencing no other housing problems and spending close to 40% of its gross income on rent would only score 12 points irrespective of income level. The Ministry argues that any family with fewer than 20 points is not really very needy. (p. 21)

It is quite possible that these criteria are consistent with some housing goal but they appear to provide an obstacle to the attainment of horizontal equity.

A second aspect of horizontal equity concerns the distribution of subsidies among tenants of public housing who are in similar economic circumstances. This dimension can be examined by comparison of subsidies received by different groups of tenants. The Canadian Council on Social Development (1977) reports that the distribution of public housing and subsidies for 1970:

> Shows that there was a considerable range of subsidies received by tenants with the same income in 1970. The range was as much as $100 a month: from $20 to $120, and this situation existed at all income levels....A further breakdown [for B.C.]...in 1975, controlling for rent levels, to see if within one rent group tenants were receiving comparable subsidy amounts...showed that for all economic rent groups the dispersion about the line of horizontal equity was considerable. For example, within the economic rent class of $120-140 a month, the amount of subsidy received by tenants with $200 income ranged from under $40 to nearly $80 a month; and for tenants with incomes in the

> $600 a month range, the subsidy received varied from close to zero to $70 a month. (p. 88)

Public housing, ironically because of its current limitations, does avoid the problem identified earlier which is inherent in housing allowances in that they direct benefits to households with current low incomes who are not an integral part of the target group. While public housing programs, in common with housing allowances, cannot avoid using current income as measures of need, the waiting period for public housing makes it less likely that households which have fluctuating incomes will either apply for or qualify for public housing if their low incomes are temporary. By the time they have worked their way up the lists to a position of priority, they will be more likely to be in a position where their current income excludes them from gaining the benefits of public housing. This force will be stronger if i) households are required to leave public housing once their income rises above the maximum support level.

4.2 The Adequacy of Housing

A public housing program by its very nature supplies accommodation to its beneficiaries. They must occupy the accommodation offered under the program in order to receive its benefits. As the preceeding analysis shows, it is premature to identify the overall effects of public housing on the basis of this evidence alone. The impact of public housing on the overall availability of rental accommodation depends on the responsiveness of private suppliers of rental housing to the level of market rents.

Evidence on the impact of public housing programs on the supply of rental housing appears to be non-existent. The use of reasonable estimates with respect to the nature of the demand for and supply of rental housing can indicate the possible magnitude of the displacement effect.

Table 6.6 below gives estimates for effects of public housing on the supply of rental housing and the level of market rates for a variety of assumptions. The results show that the displacement effect of public housing would be substantial under all sets of assumptions. In the most favourable circumstances, half the initial effects of public housing on the supply of rental housing would be displaced by a reduction of the private supply whereas in the least favourable case, over eighty per cent of the public housing would be offset through the displacement effect.

The secondary effects of public housing on market rents are also shown in Table 6.6. As in the case of the quantity effects, the calculated effects on market rents differ substantially from case to case according to the values used for elasticity of demand and supply. As would be expected, public housing would have its greatest impact on market rents when the supply of housing was least responsive to rents.

5.0 Effectiveness for Cost

5.1 Adequacy of Income

The benefits of public housing in income support to target groups accrue directly to the occupants of public housing and indirectly to other tenants, in both cases in the form of reduced rent. From this perspective, the cost

TABLE 6.6

The Effects of Public Housing on Rent and the Supply of Rental Housing: Various Assumptions

I Before Public Housing
Rent $500
Quantity of Rental Housing 1000 units

II After 100 Public Housing Units

E_s	E_d	Rent	Quantity of rental housing
.7	.7	464	1050
	.5	458	1041
	.3	450	1030
1.0	.7	470	1040
	.5	467	1034
	.3	462	1024
1.3	.7	475	1035
	.5	472	1027
	.3	469	1019
	0	450	1000

NOTE: Demand and supply functions calculated as linear approximations at initial rent and quantity of rental housing.

effectiveness of public housing requires a comparison of these benefits with the costs to government of providing them. Three issues that need to be considered are i) the household's assessment of the benefits from the lower rents resulting from the public housing; ii) the cost of public housing in relation to comparable private sector housing; and iii) the administrative costs incurred by government agencies.

The benefits from public housing programs accrue to the recipients as an in-kind payment in the form of housing services. As discussed earlier, in-kind benefits expressed at market prices are not valued to the same degree by recipients as income transfers of the same amounts. As Fallis (1980) states:

> The restriction on household choice is especially important in many housing programs in which not only is the subsidy in the form of reduced prices but also only one quantity of housing services is offered at this reduced price. There is only one housing unit offered, take it or leave it. Public housing is a program of this sort. (p. 53)

Fallis has calculated the adjustment which must be made to the market value of housing services received under public housing in order to determine the household's valuation of the benefit.

Table 6.7 shows the difference between the market and consumer surplus measures of the benefits of public housing as calculated by Fallis. The former measure captures the actual reduction in rent to typical households in each income group, whereas the latter captures the household's valuation.(3) As can be seen, the value of the benefits accruing to households are reduced substantially when

TABLE 6.7

Difference Between Market Value and Consumer Surplus Measures of Benefits of Public Housing, Ontario 1970

	Average differential benefits	
Income ($)	Market value measure	Consumers surplus measure
0 - 1,999	-520	-282
2,000 - 3,999	-172	- 71
4,000 - 5,999	270	438
6,000 - 7,999	696	889
8,000 +	---	---

SOURCE: Fallis (1980), p. 67.

adjusted to reflect the household's evaluation of this benefit.

The indirect benefits of public housing to other renters in terms of reduced market rents are more difficult to estimate. The example in Table 6.6 shows that additional public housing equal to 10% of the housing stock reduces the level of market rents anywhere from 5 to 10 per cent. Unlike the direct benefit from public housing, this benefit is available to the renters of other housing regardless of the quantity of housing consumed.

5.2 Comparative Expense

An increasing accumulation of evidence (Borcherding, 1983) suggests that public supply arrangements for any good or service are usually more expensive than comparable private suppliers for the same good.(4) Thus any review of the cost effectiveness of public housing should include an enumeration of the costs of supplying housing services through this means.

Only very limited evidence is available on the cost of supplying housing services through public supply arrangements. One of the more comprehensive studies for Canada has been conducted by MacMillan and Nickel (1974) who compare the costs of rent supplements and public housing in Manitoba. Their approach is a limited comparison of the various ways of providing housing to the 817 families receiving 100 per cent rental supplements in January 1971, for which the federal and provincial governments shared $1 million annually in expenses on a 50/50 basis.

Their calculations of the costs of public housing are based on the following assumptions:

- costs of each single detached three-bedroom bungalow of appropriate specifications would be $18,000.
- amortized over 50 years at 7 3/4% for federal government share and at 8 1/4% for provincial government share
- current operating expenses for taxes, insurance, utilities, etc., were $400,000.

On the basis of these assumptions, they estimate that the annual cost of public housing for the 817 families would be $1.6 million, or 60 per cent more than the costs of housing the families in private accommodation with 100% rent subsidies.

The MacMillan-Nickel study has been criticized by Marks (1984) on a number of grounds:

> It is not clear from the study whether the rented housing was adequate or whether the samples of public housing and supplement households were well-matched. Moreover, there is no discussion of the sensitivity of the results to the tightness of the particular housing market. (p. 79)(5)

Nevertheless Marks concludes:

> The study does lend some support to the argument that it may be more efficient to rely on existing housing. (p. 79)

In other words, public supply arrangements appear to be less efficient in providing housing at low cost than use of the private market. Public housing, by its nature, is tied to public supply arrangements. The housing allowances discussed in Chapter 4, in contrast, give the recipient households an opportunity to search out efficient suppliers.

Marks (1984), in turn, makes crude estimates of the comparison of public housing and rental supplements for Ontario in 1983. He suggests that the average household in public housing would pay $256 to $268 per month (based on an income of $12,300 to $12,900) for public housing. The average rental subsidy paid to households outside Toronto was $261, giving a total rental cost in the range $520-530 per month. Marks concludes that this figure approximates the rent which would be paid on behalf of households which cannot afford to pay any rent, the benchmarks of the MacMillan-Nickel study. Marks then compares these costs to the following rents:

Toronto - three bedroom
Controlled $478
Uncontrolled $584

- two bedroom
Controlled $401
Uncontrolled $518.

As can be seen, the cost of public housing would be less than the cost of an uncontrolled three bedroom apartment, comparable to an uncontrolled two bedroom apartment and roughly 9 to 30 per cent more than controlled apartments.(6)

The comparison used by Marks (1984) presents a bit of a puzzle. He compares the cost of public housing outside Toronto to the costs of rental housing in Toronto with only the caveat that "Outside Toronto rents would probably be lower". (p. 80) The comparison for Toronto admittedly is complicated by the fact that the subsidies are presented only for all household units rather than families alone. Using the overall subsidy figure for Toronto adds $34 to the subsidy and gives the following comparison:

Rental cost: public housing $554 - 564

Market		Cost of housing allowance as a per cent of cost of public housing
- three bedroom		
Controlled	$478	86
Uncontrolled	584	105
- two bedroom		
Controlled	401	72
Uncontrolled	518	94

Alternatively, an estimate could be made on the assumption that the ratio of subsidies to families relative to all subsidies are the same in Toronto as outside Toronto. Under this assumption the average subsidy to families in Toronto would be $372, giving the following comparison:

Rental cost: public housing $628 - 640

Market		Cost of housing allowance as a per cent of cost of public housing
- three bedroom		
Controlled	$478	76
Uncontrolled	584	93
- two bedroom		
Controlled	401	64
Uncontrolled	518	82

This final set of assumptions suggests that, as in the MacMillan-Nickel study, public housing appears to be more expensive than rent subsidies for providing adequate housing to low income households.

5.3 Administrative Expense

Little evidence appears to be available regarding the expenses that are borne by agencies of government in the administration of public housing programs. These expenses are rarely taken into account in assessing the costs of government programs. One piece of evidence is provided by Woods Gordon (1981) who pull together some scattered evidence. They report that:

> For the Community Housing Division of the Ministry of Housing direct operating costs per unit of housing produced in 1980 were estimated at $825. Costs associated with work carried out by appraisers and other M.O.H. staff outside the Community Housing Division have not been included. (p. 11)

In addition, they report that CMHC's adminstrative cost for each unit financed or supplied averaged $678 per unit, an admittedly low estimate for loans under the non-profit program. Public housing in Ontario would incur both these expenses, adding approximately $1500 to the overall cost of each unit in 1980. If these costs were added to the other capital costs of housing units, they would add approximately $10 per month to the implied subsidy.

The purpose of this discussion has been to call attention to possible cost differences between public housing and other forms of housing assistance. At most, the crude estimates are only suggestive: public housing appears likely to be more expensive than other forms of assistance. The crudeness of the estimates call for much caution. Clearly in-depth research is required to make any definitive conclusion on the issue of relative costs.

5.4 Adequacy of Housing

The second dimension of effectiveness for cost of public housing concerns the adequacy of housing aspect of the affordability and housing goal. From this perspective, public housing should be judged in terms of its impact on the size and quality of the rental housing stock.

As already discussed, a distinction must be made between the number of units supplied through public housing and the impact of public housing on the rental stock. The difference between the two measures results from the displacement effect that public housing has on privately-supplied rental housing. Thus the "benefit" measure in terms of housing availability should be measured by the net effect on the stock of rental housing. Moreover, if it were possible, account should also be taken of the type of housing displaced by the public housing. To the extent the housing market can be segmented, housing which would have been directed toward low income tenants will most likely be displaced by public housing.

6.0 Rent Gouging

Even though public housing programs are not justified in terms of their effects of rent gouging, an argument might be made to the effect that by serving as a "landlord of last resort", public housing authorities could act to restrain rent gouging whereby landlords take advantage of tenant ignorance or immobility to charge above market rents. Such an argument requires, however, that the public housing authorities i) give wide publicity of the terms under which they make housing available; and ii) have a stock of suitable housing available so that such households can switch at will. The reality of public housing in Ontario prevents it from fulfilling this role, given the lengthy waiting lists for public housing at present.

7.0 Security of Tenure

Public housing programs raise questions of security of tenure at both entry and exit. A household must physically occupy units of public housing in order to share in the direct benefits from this program. The presence of waiting lists aside, this requirement makes public housing more suitable for some households experiencing affordability and income problems than for others. Public housing would be more suitable for households that experience problems over the longer run. All households must weigh the costs of giving up their current housing in order to qualify for the benefits of public housing in the short run. But households with short term problems may be required to move once their circumstances change and they cease to be eligible for the benefits or suitability of public housing.(7)

8.0 Economic Efficiency

The benefits from public housing programs can only be obtained by occupying units in designated projects. Moreover, at present tenants cannot occupy this housing immediately at the time at which they become eligible for benefits but rather must wait until units become available, the length of the wait determined by criteria discussed earlier. Each of these features cause significant information and transactions costs for potential beneficiaries of public housing benefits.

The information costs arise because of the need for beneficiaries to determine the types of accommodation that are available, the locations of such accommodations, and to determine the conditions which must be satisfied in order to be eligible. Even in the absence of waiting lists, these information costs alone may serve to deter potential beneficiaries from attempting to qualify for public housing benefits. With the current need for rationing of public housing, the willingness and ability to overcome these costs becomes an additional, albeit implicit, criterion for eligibility for public housing benefits.

The transactions costs for beneficiaries consist of satisfying the procedures for establishing eligibility for benefits and the need to wait for appropriate units to become available once eligibility has been established. The criteria used to establish eligibility include length of residence in current jurisdiction, current housing conditions, family status, health, current burden of rent, financial commitments and current housing status. The need to endure a substantial wait in order to gain access to public housing places a household in a position of considerable uncertainty. Should it search for alternative but suitable housing within the private sector? What type of contractual commitments should it make with its current landlord? What account should it take of the prospect of obtaining public housing in making decisions about seeking employment? The fact that access to public housing is discretionary and that the receipt of benefits is tied to occupancy of a specified unit of housing makes all these questions relevant to potential beneficiaries.

Questions of recipient choice are also important aspects of the economic efficiency of public housing. As mentioned above, the receipt of benefits from public housing are not just tied to the consumption of housing services but also the consumption of housing services from a specified unit of housing. The fact that benefits are tied to the consumption of housing, as already discussed, means households value the benefits at less than their market value. This discounted value is exacerbated by the fact that the tenant's choice of housing is further constrained. The fact that the location, the size, the quality and other factors of the housing are not what the tenant would have chosen with a cash transfer equal to the same resources as required to supply the public housing reduces the value of the benefits from public housing relative to a cash transfer of equal value.

The question of tenant choice must also be considered when households' circumstances change. The tenants of public housing must face the dilemma of sacrificing the benefits from public housing in order to gain more suitable housing with respect to their changed circumstances. This lack of flexibility affects economic efficiency in a number of ways. Households may continue to occupy housing which no longer suits their needs and which may be more highly valued by other households. The efficiency effects of the lack of flexibility go beyond the effects on the efficiency of housing use. Recipients of public housing benefits may be constrained in their choice of employment if the need to change location jeopardizes their benefits from public housing. Alternatively, a change in location of employment which may otherwise lead to a change in residence may lead to excessive amounts of commuting if benefits from public housing would be lost by making a move.

9.0 Administrative Efficiency

Unlike some other housing policies, public housing requires an extensive administrative apparatus. The public housing authority must also assume the responsibility for determining the criteria for eligibility, assessing applicants according to the criteria, ranking applicants with respect to priority, notifying applicants when space becomes available and monitoring the status of tenants so as to determine the amount of subsidy for which they are eligible. Moreover, these processes impose a similar burden of supplying information and compliance on the part of the applicants and tenants. Unfortunately, direct evidence does not appear to be available with respect to these costs. It appears that they are more substantial than for a program which uses the tax system, either alone or in combination with the market mechanism in determining and distributing benefits.

9.1 Flexibility

Public housing programs must be judged as not very flexible in responding to changing needs, though some differences exist with respect to different policy goals. Public housing policies can be altered rapidly to adjust the amount of income support offered to current tenants by merely altering the degree of rent subsidy. On the other hand, the small proportion of the target group served by public housing makes it unsuitable as an instrument for changing levels of income support for the target group in general. Similarly, public housing can be only moderately effective in changing the availability of housing in a short run. Planning, approval and implementation all create substantial lags in the delivery of more housing even within a single authority. The need to gain approval of several levels of government further adds to the delay. In the longer run, any effects of public housing on the stock of rental housing will tend to be offset to an increasing degree by the displacement of private housing.

10.0 Feasibility

10.1 Level of Government

Public housing as it has been carried out in Canada has been a cooperative partnership of federal, provincial and municipal governments. This feature has been both a strength and a weakness of this program for meeting provincial housing goals. An appropriate division of responsibility has been developed under this framework. Municipal governments have been responsible for planning and development of individual projects whereas provincial and the federal governments have shared in the development of overall policies and in the financing of capital costs and operating losses.

The strength of this approach is that it places responsibility for planning at the municipal level in keeping with the Dennis and Fish (1972) recommendation:

> That housing be planned and developed by the level of government which is closest to the people - the municipal level - when housing is to be state-owned. (p. 386)

At the same time, the partnership also relieves much of the financial responsibility from the municipal level which relies primarily on property taxes for its revenues.

The present partnership does have the disadvantage that it constrains the scope for provincial government initiatives to use public housing as general social policy. To the extent the province relies on municipal governments for delivery of public housing, the program will only be able to reach households in major urban centres where establishment of a municipal housing authority would be practical. Alternatively, the provincial government must take the initiative for the planning and development aspects of public housing itself.

10.2 Adaptability to Community Needs

The Canadian Council on Social Development (1977) observes:

> The rise and fall of public housing is, indeed, one indicator of the shift in Canadian housing policy, and has coincided with growing awareness of the size of the problem involved and the costs of using this approach as its solution. (p. 69)

Similarly, any review of the literature of public housing reveals a disaffection with this policy which once played a central role in Canadian housing policy.

The Council itself identifies the main sources of dissatisfaction with public housing:

> Public housing for families has become socially unacceptable in many communities, primarily because it does concentrate many families with problems and large numbers of children into one area. (p. 160)

and

> Part of the difficulty in which the public housing program now finds itself is due to the quality of life built into the projects and the fact that they have failed to accommodate the needs and requirements of their residents. (p. 160)

These problems caused Dennis and Fish (1972) to recommend that:

> Public housing program in its present form (the construction of new, highly-subsidized units to be owned by the public and occupied only by the poor) be abandoned. Some of the reasons for doing so are contained in one review of program performance: poor locations found for residential housing; problems of design caused by cost cutting or attempts to build outstanding housing for the poor; high density, high cost housing dictated by cost concerns; insensitive management that treats public housing tenants as welfare clients; the negative attitudes of administrators, surrounding neighbourhoods, and the public generally (p. 218).

The concerns identified by Dennis and Fish may indeed be a reflection of how serious the public is about helping people with low incomes gain better housing.

10.3 Basis for Political Support

Support for these propositions put forward by Dennis and Fish has been derived from many surveys which have dealt with, in one way or another, attitudes toward public housing. Nevertheless the Canadian Council on Social Development (1977) notes:

> Few surveys or studies of public housing projects are replicated and their existence often seems to be fortuitous. Nor are different studies strictly comparable. (p. 78)

It would be beyond the scope of the present study to review the methods and results of the surveys made except to make the observation that comparison with similar surveys for market rental housing would supply a good benchmark. To what extent does the typical tenant in any housing unit find it satisfactory? Without any basis for comparison, it is very difficult to interpret the findings of these surveys.

It should also be noted that the apparent disaffection for the quality of public housing has not been accepted universally and without question. Cullingworth (1980) observed:

> There appears to be general acceptance of the Hellyer Task Force's contention that public housing projects were "ghettos of the poor; people who lived in them were stigmatized in the eyes of the rest of the community; social and recreational facilities were inadequate or non-existent; privacy was lacking and vandalism present".
>
> How representative these conclusions were in 1969, or are now in 1980, is unclear.... There is, however, evidence that bad siting and inadequate management are two frequent shortcomings - neither of which is inherent in the concept of public housing. (pp. 29-30)

Other groups are not only less willing to condemn but actually praise public housing. An Interdepartmental Study Team in British Columbia (1975) stated that the public housing program has been successful in delivering adequate shelter:

> Overall public housing subsidies provide acceptable, decent and sanitary housing in the province. (British Columbia, 1975, p. 238)

Similarly, the Association of Municipalities of Ontario observes:

> That the public housing stock constitutes a valuable resource and has provided generally good quality and affordable housing for client groups

> whose needs could not be met in the private market. (1982, p. 3)

11.0 Conclusions: Public Housing

There is little question that public housing has come into disfavour as a preferred approach to housing policy. Part of the reason for this undoubtedly arises from the criticisms outlined in the preceding section. In addition, questions of expense were likely to be important. As already noted, the scale of public housing permits it to serve only a small proportion of the target group. Public housing also has different implications for government finances than other forms of housing support. Each unit of new public housing requires governments or their agencies to raise the capital cost of this housing. While the implied government subsidy on a year to year basis may be the same as in other programs, a major part of the funding needs of public housing are concentrated at the outset. This interpretation gains some support in that the deemphasis on public housing by the federal government coincided with the development of programs which involved federal subsidies on a year by year basis for housing projects undertaken by other levels of government and the private sector.

12.0 Introduction: Non-Profit Housing

We will now turn to assess non-profit housing, the alternative which the federal government emphasized as a replacement for public housing. Non-profit housing refers to projects undertaken by private non-profit organizations or by cooperatives. Non-profit housing is considered as a form of market replacing policy for a number of reasons, though it could also be treated as a form of supply policy. The emergence of programs directed toward cooperatives coincided with the apparent dissatisfaction with public housing as a social program. Cooperative projects were typically designed to overcome the major criticism of public housing, namely, that it tended to remove recipient households from the rest of society. Co-ops permit a cross-section of households by income and other attributes within the same project.

Non-profit housing and cooperatives can be classed as market replacing because, like public housing, the motivation for development does not rest with a developer's desire for profits. Still, cooperative housing could be classed as a market-augmenting supply policy to the extent that its use depends on the response of private individuals to government subsidies. Finally, cooperatives and public housing may be treated similarly with respect to the assessment criteria for the purposes of this study.

13.0 Objectives of Non-Profit Housing

The CMHC (1983) study Section 56.1 Non-Profit and Co-operative Housing Program Evaluation (hereafter referred to as CMHC Evaluation) states that the programs:

> were designed to achieve three objectives:
> a) to provide modest, affordable housing appropriate to the needs of low and moderate income families and individuals;
> b) to produce housing at minimum costs by implementing appropriate cost controls; and
> c) to encourage approved lenders to provide capital for low and moderate income housing needs. (CMHC Evaluation, p. 2)

The CMHC Evaluation also concludes:

> There are three additional purposes for the programs implied by their design and the way they have been used.
>
> The first is to achieve income integration, or a mix of income groups within projects....
>
> The second implicit objective is to contribute to the stock of rental accommodation....
>
> The third implied objective is to contribute to the development of a housing delivery capability in the third sector. (CMHC Evaluation, p. 5)

The implicit introduction of the "income integration" purpose introduces a conflict with the objective of providing affordable housing appropriate to the needs of low and moderate income housing. To the extent that higher income groups occupy housing in non-profit and co-op programs and receive a subsidy, a smaller proportion of the benefits remain with the target groups.

This characterization of the trade-off implied by the integration objective has been directly challenged by the Co-operative Housing Foundation of Canada (CHFC) which suggests:

> The fallacy holds that all housing that is not developed for profit is social housing and that since the purpose of social housing is "To assist Canadians whose income is insufficient to gain access to adequate housing", this is the purpose of non-profit and co-operative housing". (CHFC, 1985, p. 15)

This position leads the Foundation to argue that co-operative programs should not be judged solely with respect to i) their success in ensuring a mix of income to avoid concentrations of low income households or ii) the ability to target the benefits to those who are the most in need. The Foundation protests

> These non-RGI subsidies are supply subsidies intended to deal with rental housing market realities...[and are] of the same nature and kind as direct subsidies paid out by CMHC to private entre-

> preneurs under programs such as the Assisted Rental Program (ARP) or the Canada Rental Supply Plan (CRSP) and indirect assistance given through the Income Tax Act. (CHFC, p. 15)

Notwithstanding the views of the Foundation, the position taken in this study is that the Co-op programs should be judged by the same criteria as other housing programs. The question of the distribution of benefits from housing programs among income groups remains a question of vital concern to policy makers. The choice of targets remains their prerogative. An awareness of the distributional effects of co-op housing becomes especially vital at present given the commitment to cooperative housing in the recent accord in Ontario between the Liberals and the New Democrats.

14.0 The History and Development of Non-Profit Housing

The advance of non-profit housing may be viewed as part of the reaction against public housing which occurred in the late 1960's and early 1970's. The Low Income Housing Task Force (Dennis and Fish, 1972) recommended that

> CMHC should:
> 1) Make 100 percent loans to cooperative and other non-profit institutions and groups;
> 2) Provide seed money for organization and development;
> 3) Provide technical expertise directly, through the establishment of independent advisory bodies, and by funding groups to directly supply the necessary expertise.
> 4) Adopt internal procedures which make it far more accessible and receptive to these groups. It must cultivate them in the same way as producers.
> 5) If the shelter allowance proposal is not adopted, make subsidies available for non-governmental non-profit housing and require a broad income mix. (pp. 27-28)

In addition, the move toward "third sector" housing programs reflected a desire by the federal government to achieve massive reductions in government expenditures. CMHC reports that:

> One aspect of the strategy was to replace the "capital intensive, subsidy intensive" public housing with the non-profit and co-operative housing programs.
>
> The fiscal situation of the Government and resulting cuts in spending influenced the design of the section 56. 1 programs in two ways. First, in order to reduce cash requirements, provisions were made to use private sector capital funding for loans.... Second, the section 56.1 programs were designed to provide a cap on federal subsidies.... The section 56. 1 programs offered a fixed amount of assistance for the duration of the loan, based on the difference between the market interest rate and the subsidized interest rate of 2 per cent. (45-46)

The Dennis and Fish recommendations were subsequently reflected in a changed direction in Canadian housing policy. The Canadian Council on Social Development (1977) describes this changed direction:

> The encouragement of housing developments by non-profit companies and co-operative societies, often dubbed the "third" or "community" housing sector, was a major thrust of the 1973 amendments to the National Housing Act. (p. 117)

The changes in the National Housing Act which led to this emphasis were the introduction of section 15.1 (Non-profit) and section 34.18 (Co-op) programs. These programs:

> Were designed to provide 100 per cent loans to non-profit charitable organizations, provincially or municipally owned non-profit and co-operative corporations whose intentions were to provide and operate modest housing for low and moderate income householders unable to locate or afford such housing on the open market. The loan interest rates were subsidized to 8 percent, and a 10

> percent capital contribution was provided. (Canada, 1985, Appendix 2, p. 7)

In addition, the following priorities were established: i) families of low and moderate income ii) senior citizens, and iii) special needs such as handicapped. The program was further modified in 1978 so as to reduce the current costs to the government by switching to a subsidy of operating expenses:

> Section 56.1 Non-Profit and Co-operative Housing Programs provide a subsidy to private non-profit and co-operative housing associations and provincial and municipal non-profit housing agencies.... The assistance is equal to the difference between mortgage amortization cost at market interest rates and at 2 per cent, and is first used to reduce total project cost, including amortization and operating cost, down to the lower end of market rents. The balance is used to assist low-income tenants residing in the project. (Canada, 1985, Appendix 2, p. 5)

14.1 The Extent of Non-Profit Housing

Some indication of the dimension of the change in emphasis in housing policy can be gained from quantitative indicators. By the end of 1984, some 178,000 units have been supplied through the non-profit and cooperative program combined to the total of 200,000 under public housing itself. In 1984, as Canada (1985) reports,

> 22,500 new units were committed as follows:

Public Non-Profit	5,350
Private Non-Profit	7,002
Co-op	3,574
Public Housing	1,212
Rent Supplement	1,177
Rural and Native	4,185. (p. 13)

15.0 Assessment of Non-Profit Housing Programs

Non-profit housing programs can be viewed as a continuation of public housing programs with a change in the mode of delivery. Both operate ostensibly beyond the market in that the profit motives of developers and landlords are not the initiating force. In addition, in each program, the benefit to recipients takes the form of an in-kind transfer of housing. The provision of housing services is inseparable from the benefits of the program. Thus, aside from the delivery mechanism and the decision process, non-profit programs are sufficiently similar to public housing that a complete review with respect to the criteria used in this study seems unnecessary. Instead, the assessment of non-profit housing will stress differences in the performance between non-profit housing and public housing programs.

The grouping together of a number of types of programs into the general category of non-profit housing serves to mask differences in emphasis and purpose. Cooperative housing can be considered to be the best approximation in the "third sector" to the predecessor public housing programs. On the other hand, some of the other elements of the non-profit programs appear to reflect an expression of the objectives of programs to include the supply of housing to individuals such as the handicapped or the elderly which have special needs which are difficult to meet through the private market.

16.0 Who Has the Equity?

The cooperative program under section 56.1 differs from the other programs in one important respect. In other Section 56.1 programs, rents are adjusted over time to reflect the changes in market rents which result from inflation. In effect, the equity in the program remains with the non-profit organization which sponsors the project. The higher rents can be used by the sponsor to subsidize additional housing units. In contrast, in a cooperative program, the equity remains with the occupier of the housing unit. Although the individual is unable to realize the value of this equity by selling the unit, the individual benefits to the extent that market rents on other properties increase. Membership in a cooperative, like homeownership, insulates a household from rent increases. In this respect cooperative housing programs can be considered to be treated more like subsidy programs for owned housing than like other forms of rental housing.

16.1 Who Gains the Benefits?

The CMHC Evaluation presents estimates of differential benefits by income group from the section 56.1 programs for 1980 which have been derived under the same method as used by Fallis (1980) for other programs. The data presented in Table 6.8 compares the benefits of section 56.1 programs with an equal cost program with a neutral impact across income groups. These data show that the average differential benefits from the Section 56.1 housing program relative to a neutral program were largest for the lowest income group (0 -

$4,999) and were positive for the next two income groups. All higher income groups would have benefitted more from the neutral program. Unfortunately the calculations cannot be compared directly with the estimates made by Fallis (1980) using 1971 data because of the general growth of income, both money and real, over the period.

Table 6.8 shows a comparison of the differential benefits for section 56.1 programs and public housing adjusted to be comparable with the 1980 data for section 56.1. Given the margin of error involved in the measurements and the adjustment, it appears that the two programs provide comparable benefits to recipients according to income. This measure corresponds to the vertical equity within the program.

Vertical equity, however, involves a further element of the participation by income group. A program may provide progressive benefits by income group but fail to contribute to vertical equity by being weighted toward participation of middle and upper income groups. A very different impression of the vertical equity of section 56.1 emerges from the distribution of participants by income. Households which would have had incomes below $21,000 in 1980 accounted for 95 percent of the recipients of benefits from public housing, whereas households with incomes below $20,000 made up 66 percent of the participants under section 56.1.

Finally the scope of the section 56.1 program has been very limited. Over the years 1973 to 1983, only 178,000 units have been supplied under this program. Thus from an equity standpoint, it can be argued that section 56.1 programs supply quite substantial benefits to participants

TABLE 6.8

Comparison of Differential Benefits of Public Housing and Section 56.1 Programs

Income	Distribution of Participants (%)	Average Differential Benefits Market Value	 Consumer Surplus Measure
	Section 56.1		
0 - 4999	4.0	-1453	-1134
5000 - 9999	26.6	- 509	-314
10,000 - 14,999	18.7	- 96	- 44
15,000 - 19,999	16.6	169	119
20,000 - 24,999	14.0	311	239
25,000 and over	20.1	592	427
	Public Housing (adjusted)		
0 - 6999	24	-1820	-987
7000 - 13,999	25	- 620	-249
14,000 - 20,999	46	945	1533
21,000 - 28,000	5	2436	3111
28,000 +	--	--	--

NOTE: The adjustment to Fallis (1980) multiplied all figures by 3.5, the approximate change in per capita income over the period 1970 to 1980.

SOURCE: CMHC (1983, p. 214)
Fallis (1980, p. 67) adjusted

but do not concentrate these benefits to low income groups and affect the affordability of housing for only a minor portion of target households.

17.0 Effectiveness For Cost

The cost effectiveness of non-profit and cooperative housing can be evaluated relative to a number of other programs on the basis of comparisons made in the CMHC *Evaluation*. The income mixing feature of section 56.1 makes it necessary to decide on the basis of the comparison. Should the comparison be in terms of whether subsidies should be measured per unit supplied under the program or per rent-geared-to-income unit supplied to income-tested households? The emphasis on affordable housing for present purposes means the subsidy to rent-geared-to-income households should be most relevant. Of the several comparisons presented in the CMHC *Evaluation*, the most relevant show the subsidy costs for a variety of programs under alternative assumptions with respect to interest rates. As shown in Table 6.9 the section 56.1 programs have the lowest subsidies per unit but the highest subsidies per rent-geared-to-income unit under an 18 percent interest rate. The margin per unit improves with a 13 percent interest rate, but the subsidy for each rent-geared-to-income unit remains higher than other programs with the exception of the non-profit compared to rent supplements. On the basis of these comparisons, the CMHC *Evaluation* concludes with respect to effectiveness for cost:

> When costs are considered in terms of the number of RGI units provided, the Non-Profit and Cooperative Housing Programs are the least cost-effective alternatives at an interest rate of 18 percent. At

TABLE 6.9

Subsidy Costs for Alternative Social Housing Programs with an 18% Interest Rate

	Present Value Total Subsidy	Average No. of RGI Units/Year	Present Value Total Subsidy	
			Per Unit	Per RGI Unit
Section 56.1 N/P	1,436,558	11.1	71,820	128,905
Section 56.1 Co-op	1,436,558	9.7	71,820	147,875
Section 15.1/34.18 N/P and Co-op with 44(1)(b)	1,450,774	12	72,555	120,890
Section 40 Public Housing	1,898,847	20	94,942	94,942
Section 43 Public Housing	1,898,847	20	94,942	94,942
Section 44(1)(a) Rent Supplement	1,930,263	20	96,513	96,513

1. Hypothetical Model of a 20-Unit Townhouse Project.
2. 18% Interest Rate.
3. 7.7% Inflation Rates.
4. 10% Discount Rate.

With an 13% Interest Rate

	Present Value Total Subsidy	Average No. of RGI Units/Year	Present Value Total Subsidy	
			Per Unit	Per RGI Unit
Section 56.1 N/P	938,222	10.1	46,911	92,893
Section 56.1 Co-op	938,222	8.9	46,911	105,418
Section 15.1/34.18 N/P and Co-op with 44(1)(b) Assistance	944,496	12.0	47,225	78,708
Section 40 F/P Public Housing	1,449,406	20	72,470	72,470
Section 43 F/P Public Housing	1,449,406	20	72,470	72,470
Section 44(1)(a) Rent Supplement	1,930,263	20	96,513	96,513

1. Hypothetical Model.
2. 18% Interest Rate.
3. 7.7% Rate of Inflation.
4. 10% Discount Rate.

SOURCE: CMHC, Evaluation, pp. 305-306.

> a lower interest rate of 13 percent, Cooperative Housing remains the least cost-effective but Non-Profit Housing becomes more cost-effectice than the Rent Supplement Program. (CMHC, 1983, p. 307)

18.0 Security of Tenure

Section 56.1 differs substantially from public housing, the program it replaced, with respect to security of tenure. As already discussed, public housing serves to protect tenants against economic threats to security of tenure but at the same time requires the majority of households to leave if their income exceeds the specified ceiling for assistance. Section 56.1 programs, by emphasizing a mix of incomes, provide greater security of tenure because receipt of a higher level of income does not require the household to leave the accommodation.

19.0 Economic Efficiency

Section 56.1 programs, like public housing, have implications with respect to both efficiency in terms of housing use and the impact of the programs on labour mobility. With respect to the first, when the needs of households for housing change, the programs limit the ability of the household to obtain housing more appropriate to their needs. With non-profit housing, the problem arises because the household may lose the current subsidies supplied by the program by moving elsewhere, unless there is an abundance of subsidized accommodation.

The problem is somewhat more substantial for co-operative housing. The member of a cooperative receives a property right in the form of virtually unrestricted tenure in an assigned unit of the cooperative project. The right to this tenure approximates that of a homeowner in all but one respect. The owner of a house is able to sell his property right to a house and use the proceeds to purchase another house. Thus the homeowner is able to adjust housing requirements to needs. A household in a cooperative has property rights only to occupy the unit on terms set for the cooperative as a whole. If the household leaves the co-operative, all rights to the benefits are forfeited. This cost will be particularly severe after a period of inflation because all the costs of the cooperative except the operating costs would be based on historic costs from the time the cooperative was formed.

Any household considering a change in the quantity or quality of their housing must face the prospect of forfeiting the benefits of the co-operative in order to move. This property right feature serves as an obstacle to efficient use of the housing stock. In addition, it serves as an impediment to labour mobility. Households may refuse up opportunities for superior employment to the extent that such employment requires the surrender of housing benefits obtained through membership in a housing co-operative.

20.0 Income Mix

The section 56.1 programs differ from their predecessors to the extent that the goal of "income integration" gained some emphasis. Statistics shown earlier suggest that section 56.1 programs provide assistance to a wide spectrum of incomes. This evidence, however, does not indicate how well incomes are integrated on a project by project basis. The

CMHC _Evaluation_ provides the data presented in Table 6.10 on the proportion of households which are assisted in a sample of 178 projects. The two categories, 0 per cent of assisted households and 100% of assisted households, together are interpreted as indicating absence of income mixing. The CMHC _Evaluation_ observed:

> About 29 percent of all projects examined had no assisted households while all households were assisted in about 16 percent of the projects. Thus, no income mix was evident in about 45 percent of the projects examined. These projects, however, accounted for only 23 percent of all units in the projects under scrutiny, indicating that zero income mixing occurs most frequently in small projects. (CMHC, 1983, p. 166 and 168)

The CMHC _Evaluation_ continues:

> The question of whether the degree of income mixing achieved in these projects is acceptable is difficult to address since the programs do not specify an acceptable range in the percentage of assisted units for which projects should strive. (p. 168)

Program manuals suggest that the cooperative groups should strive for 15 percent assisted households. The CMHC _Evaluation_ sets an acceptable range from 11 to 50 percent and concludes that 35 percent of projects fall within the range. Those projects tend to include larger projects and more of the family projects than senior citizen projects.

A final aspect of the income mix of section 56.1 is the setting of rents at the lower end of market. This provision reflects a concern with attracting households with moderate and higher incomes so as to achieve a mixing. If rent levels are set too high, projects would find it difficult to attract higher income households. Too low rents, on the other hand,

TABLE 6.10

Distribution of Section 56.1 Projects According to the Percentage of Assisted Households Within a Project, by Project Type

Percent of Households Assisted	Family			Senior			All Projects		
	Number of Projects	Percent of Projects	Percent of Units	Number of Projects	Percent of Projects	Percent of Units	Number of Projects	Percent of Projects	Percent of Units
		%	%		%	%		%	%
0	40	27.7	8.4	12	35.3	34.4	52	29.2	15.0
1 - 10	7	4.9	18.9	0	0	0	7	3.9	14.2
11 - 15	6	4.2	8.0	2	5.9	14.9	8	4.5	9.7
16 - 25	28	19.4	27.8	1	2.9	2.2	29	16.3	21.3
26 - 50	21	14.6	19.3	5	14.7	10.3	26	14.6	17.0
51 - 75	11	7.6	6.0	2	5.9	2.5	13	7.3	5.1
76 - 89	8	5.6	4.7	4	11.8	10.3	12	6.8	6.1
90 - 99	2	1.4	1.6	1	2.9	9.9	3	1.7	3.7
100	21	14.6	5.3	7	20.6	15.5	28	15.7	7.9
Total	144	100.0	100.0	34	100.0	100.0	178	100.0	100.0

SOURCE: CMHC, Evaluation, p. 167. Derived from Section 56.1 Project Managers Survey.

lead to too much of the project subsidy being directed away from the target groups. The CMHC Evaluation concludes:

> An appropriate range for the "lower end" of market rent is arbitrarily selected as 85 to 95 percent of the average market rent. (p. 170)

The CMHC _Evaluation_ compared i) the low end of market rents on the sample of section 56.1 projects with market rents for selected cities and ii) the low end of market rents for 1981 projects with the 1981 market rents for newly constructed buildings. These comparisons for Ontario cities, presented in Tables 6.11 and 6.12, do not show any consistent pattern. The existing projects have a wide variance but on average 87.8 percent of rents fall within the range. On the other hand, the new projects, which average 78.5 percent of market rents on new structures, fall distinctly below the acceptable range. Finally, the CMHC _Evaluation_ surveyed project managers with respect to their judgement about the lower-end of market rents (LEMRs) in their projects relative to market rents. They report that:

> In Ontario, over one-half of the project managers indicated that LEMRs were about the same as market rents. (p. 173)

On the basis of this mixed evidence, the _Evaluation_ concludes:

> The initial analysis on the lower end of market rent found that only 30 percent of LEMRs were within 85-95 percentage points of the average market rent. Based on project managers' perceptions, this would increase to 45 percent. The objective data indicated that in close to 50 percent of the cases examined, LEMRs were less than 85 percent of market rent. The implications of this finding are that non-income-tested occupants are receiving subsidized rents in these projects in

TABLE 6.11

Comparison of Lower End of Market Rents to Market Rents in Selected Cities, Ontario

City	No. of Bedrooms	Lower End of Market Rent $	Market Rent	LEMR as a % of Market Rent %
Brantford	2	404	295	137.0
	3	374	355	105.0
Hamilton	2	285	312	91.3
	3	338	392	86.2
Oshawa	1	240	307	78.2
	2	304	341	89.1
	3	305	411	74.2
Ottawa	1	281	318	88.4
	2	321	394	81.5
	3	457	493	92.7
Thunder Bay	3	391	380	102.9
Toronto	1	283	339	83.5
	2	313	403	77.7
	3	606	479	126.5
Mississauga	1	252	343	73.5
	2	314	407	77.1
	3	357	470	76.0
Brampton	2	400	354	113.0
	3	460	396	116.2
Windsor	1	175	281	62.3
	2	205	361	56.8
	3	295	530	55.7
Peterborough	3	264	358	73.7

SOURCE: CMHC, Evaluation, p. 171. Derived from Section 56.1 Occupants and Project Managers Survey and Statistical Services Division.

TABLE 6.12

Comparison of Lower end of Market Rents by CMA to Market Rents for Newly Completed Structures, 1981 (Commitment Data)

CMA	Row, 3 Bedroom Unit			Apartment, 2 Bedroom Unit		
	LEMR $	Market Rent $	LEMR as a % of Market Rent %	LEMR $	Market Rent $	LEMR as a % of Market Rent %
Hamilton	415	455	91.2	390	550	70.9
London	395	450	87.8	365	395	92.4
Ottawa	415	600	69.2	363	510	71.2
Toronto	510	650	78.5	439	550	79.8

SOURCE: CMHC, Evaluation, p. 172. Derived from CMHC Section 56.1 Administrative Data and CMHC Appraisal Staff.

> order to achieve the desired income mix. It should be noted that this finding is not supported by the perceptions of project managers, only 17 percent of whom felt that LEMRs were much lower than market rents. (p. 175)

The comparisons have a number of shortcomings. The CMHC Evaluation notes that the treatment of utility expenses may not have been uniform in the comparisons. Equally disturbing is the inability to compare comparable quality units. Are moderate and upper income groups in section 56.1 paying low-end of market rents for average, below average or above average accommodation? Without this information, the degree of subsidy to moderate and upper income groups in section 56.1 projects is difficult to determine.

21.0 Conclusion: Non-Profit Housing

In summary, non-profit programs appear to have been initiated as a reaction to criticisms of public housing to the effect that low income tenants were effectively segregated from the rest of society with resulting attendant ill effects. Without question, non-profit and cooperative housing have achieved a greater mix of incomes than possible with public housing but only at some cost with respect to other goals. Projects under these programs generally subsidize all tenants to some degree in order to achieve rents at the lower end of the market. Such subsidies divert resources away which could have been used to the benefit of target groups for redistribution. In most other dimensions, non-profit housing shares the virtues and limitations of public housing. Its effects on the adequacy of housing cannot be determined without measurement of the possible displacement effect; it cannot counteract gouging; and it can lead to inefficient use of housing and other resources. However, non-profit housing has served as an important mechanism by which households and individuals with special needs, such as the handicapped and elderly, can meet their housing requirements.

Notes to Chapter 6

(1) Note that the increase in supply of rentals must be completely unexpected to give this result. If the public housing were anticipated, private suppliers would reduce the quantity of private rentals on the market. As discussed in the text, this displacement effect would be most likely in a growing market where public housing would discourage the projects planned by private suppliers.

(2) Once again, the reader is reminded of the evidence presented in Appendix 1 to Chapter 7 which suggests that rental housing can be expected to be price responsive.

(3) Consumer surplus measures the valuation that the recipients attach to the additional housing. Conceptually it represents the maximum amount that they would pay for the housing if they had the choice.

(4) It should be noted that the nature of the good provided by public suppliers may not correspond to the good supplied publically. Thus, in many instances, this criticism does not apply.

(5) In addition to these criticisms, it is not clear that MacMillan and Nickel consider any administrative costs from operating the programs.

(6) However, the estimates are based on average market rents which may overstate the rents on units of comparable quality to public housing.

(7) In public housing with 100 percent rent-geared-to-income units, tenants are required to move out once their incomes reach a certain level. There is a provision for up to 10 per cent of these tenants to stay, in which case they are expected to pay up to a low end of market rent.

CHAPTER 7: A COMPARISON OF THE ALTERNATIVES

by Kelly Busche and John Chant

1.0 Introduction

Up to this point of the study, specific housing policies have been examined one at a time in isolation from each other. The choice of evidence has, in large measure, been governed by expediency. In some cases, actual programs have supplied the relevant evidence, though different programs may be used for different dimensions. In other cases the evidence has been derived from experiments. A major difficulty arises from this approach; the evidence has not been developed from programs of comparable size. Unfortunately, the scope of experience with housing programs has not produced the types of evidence needed to produce appropriate comparisons among programs. Still the fact remains that policy makers must decide among programs of comparable expense.

The present chapter supplies an alternative approach to the comparison of alternative housing programs. Policies of comparable size are simulated in order to determine their effects. The simulations are made in each case using the most likely estimates of the market factors which will determine the effects of the policy. In addition, a variety of estimates of crucial values are used in order to demonstrate the degree to which the results are dependent on the assumptions that have been made.

Some caution must be added with respect to the final product which is produced from these simulations. It is not offered as a definitive description of what may happen if any policy is introduced. Rather, we provide it for the purpose of adding to, supplementing and reinforcing the analysis of the preceding chapters.

2.0 The Method

In this chapter, the different alternatives are examined on an "equivalent" basis. That is, we estimate the effects of the different policies on the assumption that the same conditions exist in the market for each policy, and that each policy has the same amount of financial commitment from the government. As in the case of the first chapters of the study, we focus on the three basic questions: what are the effects on income distribution? what are the effects on rent levels? what do these effects imply about the supply and consumption of rental housing in the market? By examining these issues across "equivalent base" policies, the resulting comparisons allows policy makers to make judgements with the knowledge of which programs provide the "biggest bang per buck" for a given objective. It will be seen that different policies will be differentially effective for different objectives: some will relatively more effective at distributing income to the target households while others will be relatively better at increasing the quantity of housing services consumed by these households. Which trade-offs between objectives are acceptable and which are not are questions to be settled by the policy makers and politicians but not us.

2.1 Definition of Equivalent Base

The policies considered in this study differ in one important dimension for the purposes of this head-to-head comparison. The demand augmenting and supply augmenting policies to be examined all provide assistance in the form of annual flows. Public housing, in contrast, requires a capital expenditure which would not be required by the other programs. To make it possible to consider these programs under the assumption that expenditure is the same for all, the capital cost plus annual operating expenses associated with the public housing option has to be made equivalent to the annual cost of the other programs. To make the two expenditures the same, it was assumed that the government would build housing and, from the market rent, would subtract a subsidy equal to the cost of the other programs. The capital cost is just the discounted value of the income flow so the amount of annual subsidy is the cost. In this way, the capital cost becomes irrelevant for comparison purposes and the relevant figure is the annual subsidy. This method makes irrelevant who builds or owns the actual housing.

The second part of the definition of "equivalent base" relates to the fact that different programs are likely to take different amounts of time before they are finally implemented. For example, some programs may be simple enough that little "learning period" is required before all eligible households who want to participate are actually in the program. For other programs, however, the participation rate is expected to rise over the start-up period so that the program might not be fully implemented for many months or even several years. To ensure that we examine the alternatives on the basis of equivalent funding expected for the fully implemented program, all calculations of costs and levels of assistance are done for the fully implemented program. This, of course, means that some programs will be somewhat less expensive for the start-up period, even though they will be equally costly when operating fully.

For the purposes of calculations in this study, the equivalent base of expenditure is set at two hundred million 1983 dollars. The $200 million figure is arbitrary, but the analysis is carried out in such a way that if a larger program were preferred, then most of the impacts can be scaled -- a three hundred million dollar program will have one and a half times the impact, etc. Where specific impacts cannot be scaled in this manner, the appropriate caveat is added.

2.2 The Programs to be Examined

a) Unconstrained demand assistance

All households with incomes below some set level, either the Statistics Canada Revised Low Income Cut-Off (RLIC) or one and a half times that level, will be eligible for assistance. Assistance will be given as a proportion of the difference between 25% of income and an average rent level for household size and rent level of that household's location.(1) The program is unconstrained in the sense that only average rents for household size and location are relevant for determining assistance; whether a household chooses to consume more or less than 25 (or 30) per cent of income on rent is irrelevant. Households neither receive less if they choose accommodation which is relatively inexpensive (relative to similar accommodation) nor will they receive more by choosing relatively more expensive accommodation.

b) Constrained demand assistance

This program is similar to the unconstrained version except that assistance will be a function of actual rent paid rather than some average level. Households of similar size, income and location will receive more assistance if they spend larger proportion of income on rent. On the other hand, households which spend less than 25% on rent will be ineligible for assistance whatever their income. This will, of course, make it profitable for them to increase their expenditure on rent. Because of these features, the assistance available must be additionally constrained not to exceed some absolute level.

c) Supply side assistance

Supply subsidies are attached to specific rental units and a government agency would assign low income households to these units.

d) Public housing

In this program, publicly owned rental units would be assigned to low income households. The amount of the subsidy is the difference between market rents and those charged by the public housing authority.

2.3 Target Households

As a first approximation, we assume that rental families with incomes at or below one and a half times the Statistics Canada Revised Low Income Cut-Off (RLIC, see Table 7.1) will be eligible for assistance. Households with incomes below 1.5 RLIC number about 157 thousand of the 1,100 thousand rental households in Ontario. More restrictive eligibility

TABLE 7.1

Revised Low Income Cut-Off Levels (1983)

Household Size	Urban Centres Population > 500,000	Urban Centres Population 30-500,000	Rural Centres
1 person	$9,429	$7,766	$6,973
2 persons	$12,440	$10,221	$9,113
3 persons	$16,641	$13,710	$12,203

SOURCE: Statistics Canada, "Income Distribution by Size in Canada". 1984.

rules could be used, for example, 145 thousand households have incomes below RLIC and of these, only 125 thousand typically spend more than 25% of income on rent.(2) It will turn out that even using the most broad category, all households with less than 1.5 RLIC, assistance levels would be quite large, up to about $1,600 per year per household. In view of this, the largest figure is the one generally used. Another reason for using the larger figure relates to the incentive effects some assistance programs are expected to have. For some, possibly a small number of households, the assistance program will result in increases of rent expenditure (if the assistance is constrained), and or reductions in reported or actual income, for the purpose of gaining eligibility. Using numbers which are better considered "upper bounds" will make the estimates of impacts biased somewhat in the direction of more assistance per dollar of governmental expenditure. For example, using a "too large" number of eligible households will imply that the above noted $1,600 per year per household could be achieved at a cost somewhat less than $200 million per year.

2.4 Participation Rates of Eligible Households

An important part of estimating the effects of any assistance program is, of course, knowing how many households will participate. While we have used the figure 157,000 as the number of households eligible, experience in assistance programs in British Columbia, Manitoba, and the United States suggests that only a portion of eligibles will participate. Steele (1984, 1985a) suggests that about 60% is a reasonable participation rate. This number is broadly consistent with evidence from the above noted programs but for reasons we discuss below, a significantly higher proportion of 80% is used here.

There are reasons why the observed participation rates from B.C. and Manitoba and most U.S. programs are likely to be underestimates of the participation rates in a permanent assistance program in Ontario. First, many programs from which the observations were gathered were temporary programs or the information was gathered during the early stages of the programs when certain "teething" problems were experienced. Both of these considerations would tend to produce underestimates of participation rates relative to those which would be expected for permanent programs which were in a fully implemented stage.

The temporary programs can be expected to involve smaller proportions of eligible households because the temporary nature reduces the benefits derivable. Since costs to eligible households, filling in forms, finding out about the programs, showing tax returns, producing receipts for rent paid, etc., are mostly independent of the duration of the flow of assistance benefits, shorter-lived programs are less profitable and, hence, fewer eligible households can be expected to participate. Steele (1985a) for example, estimates that more than 10% of eligible households did not participate in the Manitoba Supply Assistance for Elderly Renters (SAFER) program either because benefits were too small (4.9%) or "it was not needed" (5.4%).(3) Since longer-lived programs have higher benefits relative to costs, the first group can be expected to shrink and while greater benefits may be "needed" less than smaller benefits, even some who said they didn't "need" the smaller levels of assistance can be expected to participate when larger benefits are available.

In addition, it takes time for all eligibility criteria and benefit availability to become well-known. For this reason, the participation rates of assistance programs can be expected to grow over time until they reach some stable maximum level. Evidence of this view is available from other findings related to the Manitoba SAFER program. More than 35% of eligible households failed to participate because of some misunderstanding relating to the program: 10.3% confused the SAFER program with other programs; an additional 10% incorrectly thought their incomes too high; 10.7% did not apply because of administrative problems such as being sent the wrong forms, or they considered the forms too complicated, etc.; and 4.2% incorrectly thought that the assistance was taxable.(4) Both administrative problems and confusion on the part of eligible households can be expected to diminish over the period of the program's operation and would thus increase the observed participation rates.

Another consideration which suggests that observed participation rates for temporary programs or newly implemented programs will provide underestimates of the participation rates which might be expected for a permanent Ontario program in full operation is the mobility of eligible households. For the period 1978-81, between 10 and 20 per cent of program participants of B.C. and Manitoba had moved in the previous year.(5) Slightly older data (1974) shows that more than 25% of households with incomes below 1.5 RLIC had moved within the previous year.(6) Both those households moving in and those moving out are less likely candidates for participation since, on the one hand, it will be costly to learn about programs in new areas, and on the other, the prospect of moving out of an area reduces the expected benefits of an assistance program.

Finally, some support for using a rate higher than 60% (or thereabouts) is found in the experience of the Experimental Housing Allowances Program (EHAP) in the United States. Even for temporary programs, rates in excess of 80% were observed for unconstrained programs.(7)

3.0 The Effects of Unconstrained Demand Assistance

3.1 The Assistance Formula

Eligible households are those whose incomes are below 1.5 times RLIC. Assistance would be a proportion of the difference between 25% of income and the "average rent" for a household of given size and location. "Average rent" is defined in detail below.

The assistance formula is therefore:

$A_i = [R_i^* - .25\ Y_i]$ times the contribution proportion, x.

A_i is the assistance to household i; $\overset{*}{R_i}$ is the "average rent" for household i, given the size of household and its location in terms of average rent levels. Households in relatively higher rent areas would receive greater amounts of assistance than those households in relatively lower rent areas. By adjusting for the average level of rent in different locations, the program would be neutral in terms of its incentives for moving from one rent location to another. If no adjustment were made, that is, if R* were the same in high and low rent locations, households would find it profitable to move to low rent locations since disposable income after payment of rent would increase relative to higher rent locations. The adjustment for size of household implies simply that non-income earning household members such as children and the elderly increase the amount of assistance for a given household.

As an example, a three person household with income of $12,000 which resides in an area where "average" rent for that household size is $4,800, would receive a fraction of the "gap" of $1,800 [$4,800 - .25($12,000)]. If the assistance rate were set at 75%, the household would receive $1,350 per year. A single individual with similar income but who, because of a smaller household size, faces "average" rent of only, say, $3,600 would receive 75% of only 600 dollars, or $450 per year.

3.2 Assistance per Participating Household

Using the 80% participation rate, and using 157,000 households as the number of "target" or eligible households (those with incomes below one and a half times RLCI), there will be 126,000 participating households. On average therefore, the $200 million (1983 dollars) per year funding will provide $1,587 per household per year. The formula provides for larger households receiving more for given income and location (rent level), and lower income households receiving more for given size and location. While households in higher rent areas will receive more assistance, there is no incentive for average households to move to higher rent areas since the higher assistance will be equal to the higher rent payments. Total after rent income for a participating household is, therefore, independent of the average level of rent in any location.

To get an idea of how much individual households would receive, consider three households:

i) single person over 65, \$7,885 (1983) income(8)

ii) two person household, no children, \$13,089 income

iii) two plus person household, both spouses present, youngest child over 6 years, \$17,347 income.

The first household (facing an average rent of \$4,068) would receive a proportion of the difference or "gap" between the average rent and 25% of income (4068 - .25(\$7,885) = \$2,097). For the second household, with rent of \$5,040, the resultant gap is \$1,768. For the third household with rent of \$5,752, the gap is \$1,415.

Assuming that each of these households is approximately equally represented in the population of participating households and assuming that these three households approximate the distribution, then the average gap is \$1,759 (for 1983). Distributing the \$200 million over 126,000 households yields \$1,587 per household, or 90% of the gap. Using 90% as the assistance rate, the single person household would receive \$1,887, the two person, no children household \$1,591, and the two plus person, both spouses present, children over 6 household \$1,274. These calculations are done on the basis that rents are equal over all locations or that there is no adjustment made for differential rents in different locations. These figures are summarized in Table 7.2

If we assume that the difference between rents in (only) two types of rent locations is 25%, then those households in higher rent areas would receive higher payments as shown in Table 7.3

On an absolute level of assistance basis, Table 7.3 shows that low income elderly singles in high rent areas would receive relatively large amounts of assistance (approximately \$175 per month), while higher income, larger households in low rent areas would receive substantially less, approximately \$100 per month.

As a final example, we could examine the third family with two lower income levels, \$10,000 and \$13,000, and which face average rents. With \$10,000 of income (about 73% of RLIC for 3 person households in centres of population, 30-500,000) and \$5,752 rent payments, assistance would be (\$5,752 - 0.25(\$10,000)) 0.90 = \$2927 or about \$245 per month. At a nigher income of \$13,000 (approximately equal to RLIC for 3 person households in centres of population, 30-500,000), assistance would be somewhat less at \$2,252 or about \$190 per month.

While these assistance payments are fairly substantial, the unconstrained nature of the program allows households to spend them on goods and services (other than rent) as they choose. The extent to which these payments will be spent on increased housing services is discussed in the next section.

TABLE 7.2

Income, Rent and Assistance Levels*

Household	Income	Rent	Assistance
Single, over 65	$ 7,885	$4,068	$1,887
Two persons, no children	$13,089	$5,040	$1,591
Two plus persons, both spouses present, youngest child > 6	$17,347	$5,752	$1,274

* based on $200 million distributed to 126,000 households, 90% assistance proportion.

TABLE 7.3

Income, Rent, and Assistance Levels; Adjusted for Different Rent Locations

		Assistance	
Household	Income	Low Rent Area	High Rent Area
Single over 65	$ 7,885	$1,651	$2,123
Two persons, no children	$13,089	$1,392	$1,789
Two plus persons, both spouses, children > 6	$17,347	$1,115	$1,433

3.3 Increased Housing Expenditure per Participating Household

On average, participating households will receive $1,587 of additional income. This would be just less than 10% of 1983 RLIC income for a 3 person household, living in a large urban centre. Estimates of the proportion of extra income spent on housing range from a low of 0.06 to a high of 0.19(9), that is, an extra thousand dollars of annual income will result in between sixty and one hundred and ninety dollars of extra expenditure on housing. On average, the $1,587 will then result in between about one and three hundred dollars of extra expenditure on housing. However, while the average is between one and three, that group of households with the lowest income and the largest number of members will spend up to nearly $600 per year extra on housing.(10)

The increases of between about one and six hundred dollars per year in housing expenditure represent only about 8% more expenditure for participating households currently spending $350 per month. This 8% (average) increase in housing expenditure does not necessarily translate into 8% more quantity or quality of housing for participating households. Some of the 8% may be taken up in the form of increases in rent which are occasioned by the increased pressure on the rental market generated by the assistance program. The extent to which the extra expenditure will provide extra housing, either in terms of quantity or quality, is discussed in the next section.

3.4 Increased Housing Consumption

Estimating that participating households will increase housing expenditure by between six and nineteen dollars per hundred dollars of assistance implies a total increase in housing expenditure by recipient households of between 12 and 38 million dollars per year. To know whether this increase in expenditure will result in higher rent prices, two key issues must be examined: first, how the assistance program will be financed, and second, how suppliers of rental housing will react to any increase in demand for rental housing.

The means of finance is important to the question of the degree to which increased expenditure by recipient households will be translated into increased housing consumption rather than increased rent prices. At one extreme, if the program is financed by taxing relatively higher income households with the same "tastes" for housing, then there will be no impact on prices since the extra 12 to 38 million dollars spent by recipient households will just be matched by a similar decrease in housing expenditure by financing households.

Two other possibilities exist. First, we could assume that there will be no reduction in the housing consumption of financing households in response to the lower income after tax. Alternatively, we could assume that financing is accomplished through some reduction in other programs such that after tax income of the community as a whole is not affected and housing demand by non-recipients is not changed. It is useful to examine the program on this basis since it provides the opposite extreme from the case where housing expenditure is shifted from financing to recipient households but not changed in aggregate. Under this assumption, the maximum price increase for given supply conditions can be calculated. This will put a lower bound on the amount of increased housing consumption as opposed to expenditure.

We use five estimates of supply elasticity: zero, 0.3, 0.7, 1.3, and infinity. For zero elasticity, increases in expenditure are observed as increases in price only there is no increase in the net stock of housing; for 0.3, 0.7 and 1.3, there is some increase in prices, and for infinite elasticity, there is no price increase -- all of the extra expenditure is absorbed in additional housing while prices remain the same. As will be seen, which assumption is chosen is not of great relevance to recipient households since increases in rental prices will never be such that a significant portion of the assistance is taken up in prices rather than increased accommodation.

To calculate the greatest price impact possible for recipient households, we assume that supply elasticity is zero, the maximum 38 million dollars rather than the minimum 12 million is spent on housing. Under these assumptions, expenditures on rental housing at the initial rent levels increase by $38 million on a base of $5 billion, or less than one per cent.(11) The increased demand from recipients households puts upward pressure on rents which, given the assumed inelastic supply curve, can be alleviated only by reduced demand from other tenants. The ultimate effect depends on the elasticity of demand. Rents would go up by one per cent if the elasticity of demand for rental housing were unity and by 1.2 per cent if the elasticity of demand were 0.8. In either of these situations, the $38 million of extra expenditures translates into about 10 per cent more housing for recipient households.(12) On the part of the financing households, the one per cent increase in rental prices implies a loss of income of about $50 million per year above their increased taxes. This $50 million from financing households plus about $4 million from recipient households will be passed to landlords as higher rent.

To reiterate, if we make those extreme assumptions which produce the highest possible price increases and therefore the least possible increase in housing services consumed by the target households, the results are:

- up to a 1.25% increase in rental prices,
- about a 10% increase in housing consumption by target households,
- about $54 million of extra rent passed to landlords ($50 million from financing households and $4 million from recipient households),
- increased federal and provincial tax revenues because of higher taxable income of landlords,
- financing households will pay an extra $40 million over and above the $200 million for the program.

On the other hand, if we assume that supply is elastic or that financing households reduce their expenditure on a one to one basis with increases in expenditure by recipient households, the results are:

- no increase in rental prices;
- marginally more than a 10% increase in housing services for target households;
- no income loss by financing households through higher rent;
- either a 10% increase in the stock of housing of the target households (supply elasticity of infinity), or

an average reduction in housing expenditure by financing households of approximately $60 per year.

3.5 Summary of Unconstrained Demand Program

- eligible households: 157,000 renter households with incomes below 1.5 RLIC
- participating households: 126,000
- average increase in incomes: $1,587 per year. This is 90% of the average "gap" between 25% of income and average rent.
- average increase in housing expenditure/consumption: about 9 to 13% increase in expenditure (trivially less for consumption) for recipient households; for financing households, about one per cent less consumption at average rents of $500 per month.
- increase in total rental housing stock: between zero and one per cent increase, depending upon assumed supply response.

4.0 Constrained Demand-Side Assistance

4.1 The Assistance Formula

The general formula for assistance for the constrained program is the same as for the unconstrained version except that instead of the average level of rent being used, actual rent payments are used. Again, the difference between 25% of income and rental payments makes the "gap", some proportion of which will be provided as assistance.

The most important implication of this program which differs from the unconstrained program is an implicit penalty for households which prefer to consume less than the average quantity or quality of housing. Moreover, those households which prefer relatively more or higher quality housing receive a subsidy to do so. For example, a household with $10,000 income which spends only $2,500 on rent would receive no assistance, whereas, using a 75% assistance rate, a household which spent $3,700 on rent would receive $750 in assistance per year. That is, for an extra $250 per year expenditure of its own, an eligible household could increase its housing consumption by $1,000 or about 40%.

Another important implication, different from the unconstrained program, is that the program using actual rent payments includes an incentive for households to move to more expensive locations when the higher rent expense reflects better locational attributes (rather than better accommodations alone). For example, living nearer a subway stop in Toronto is valuable and if actual rental payments determine assistance levels, then households could move between two equal size and quality accommodations but with different subway access and part of the difference in rent would be paid through the assistance program, according to the rate of assistance. No judgement is intended whether this is "good" or "bad".

4.2 Assistance per Participating Household

The static estimates for a constrained allowance program will exceed those of an unconstrained program with the same level of assistance and the same threshold level of income for several reasons. First, the increased level of assistance that is paid to households which make relatively large expenditures on housing may not be offset completely by the reduced payments to others.(13) Second, the constrained allowance reduces the effective price for rental housing and creates an incentive for households to increase their expenditures and, as a result, their total assistance. Both these elements make the cost of a constrained housing allowance higher than an unconstrained allowance of the same dimensions.

The analysis to this point has been conducted under the assumption of a $200 million commitment to each program. Clearly a constrained allowance with a 90% assistance rate and a 25% rent-to-income threshold would cost more than $200 million. A comparable program designed to limit the cost to $200 million would require either a lower rate of assistance or a higher threshold for rent-to-income in order for households to qualify for assistance.

Any number of assumptions could be made with respect to assistance rates and threshold levels to give a constrained housing allowance which costs $200 million. The choice of combinations will determine the effects of the program. A high threshold which excludes many households permits a higher rate of assistance for any given housing gap and will create stronger incentives for increased housing expenditure than a program with a lower threshold and a lower assistance rate.

The choice between assistance rates and thresholds for assistance alters the effects of a housing allowance. Two extremes can be identified. The one with least effect uses the same (or even higher) threshold but must of necessity have an assistance rate of zero -- in effect, an unconstrained allowance. At the other extreme is a program with a threshold set at a level which gives a static expense equal to zero. The expense of this program arises solely from the induced effect on expenditure for rental housing.

While this extreme case is unrealistic, it supplies a useful benchmark by indicating the maximum effect that a housing allowance would have on housing consumption.(14) The results from this case must be judged as the extreme effects that a housing allowance can have on housing expenditure and the consumption of housing.

4.3 Increased Housing Expenditure per Participating Household

In the unconstrained program, households increased their consumption of housing services purely through the increase in income occasioned by the assistance (average) of $1,587 per year. The constrained program gives an added incentive since the effective price of housing is reduced to a significant degree by the fact that assistance is based upon actual rental payments. On the margin, rent for a low income household currently paying 25% of income will fall by the proportion of the gap which is covered by the assistance program. In the example of a $10,000 income household paying $2,500 per year with assistance rates of 75%, an extra $1,000 of rental payments included an additional cost of only $250 or about 25% of market costs. If an extra room in an apartment costs about $90 per month, then the effective cost to assisted households would be only about $22.50 per month.

Estimates of the demand elasticity (at a point) for housing range around 0.4 to 0.8. That is, a ten per cent reduction in rental costs is expected to result in a 4 to 8 per cent increase in the expenditure on housing, income held constant. If we assume that the income effects for participants in the constrained program are similar to those for the unconstrained program, then the income effect implies an increase in housing expenditure of between one and three hundred dollars per year. Using an assistance rate of 75%, then to the income effect must be added the impact of marginal rent costs falling by 75%. For households just on the margin, that is, currently paying exactly 25% of income on rent, this reduction in effective cost implies a large increase in housing expenditure of between 30 and 60 per cent using the 0.4 and 0.8 demand elasticity estimates. Point elasticities, however, are technically valid only for "small" changes so the 30-60% figures may be higher or lower than what would be calculated using average elasticities.

For households not exactly on the margin, the price reduction is somewhat different. For example, if we consider a household with income of $10,000 which pays only 20% in rent, increased expenditure of $1,000 per year (from 2 to 3 thousand) will attract assistance of only $375 (0.75(3,000-0.25(10,000)). Thus, the decrease in price is only about 37.5%. On the other hand, if we consider a similar income household currently paying more than 25%, the reduction will be equal to the contribution rate (75% in these examples) but will increase the income effect since current housing consumption becomes less expensive.

To get an idea how important the price subsidy effect will be, it should be noted that, for 1980, of those households with incomes below 0.5 RLIC, 98% paid in excess of 30% of income in rent; and for those with incomes between 0.5 RLIC and 1.0 RLIC, 89.6% paid more than 30%.(15) This implies that the vast majority of participating households will observe a rent reduction of the assistance proportion and many will have income effects additional to the initial assistance.

Several problems should be highlighted before proceeding with any estimate of the increased housing under this program. First, and already noted, the number of eligible households which will participate is difficult to determine; some may not participate because of the higher costs involved with providing documentation of rent payments, others may participate by obtaining fraudulent rent receipts, and some may not participate because of the requirement that at least 25% of income must be paid out in rent before any benefits can be derived. On the other hand, some households whose incomes provided only small benefits under the average rent unconstrained program could achieve higher benefits under the constrained version. For example, using a 75% assistance rate, a family with $16,000 income where average rents are $4,000 would receive nothing under the unconstrained program. Under the constrained program, they could increase their housing expenditure by $1,000 per year at a cost of only $250 (at 75% assistance rate), and hence would be more likely to participate.

For reasons of simplicity, and in order to make the comparison among programs somewhat easier, we assume that the net effect is zero, that is, the number of households encouraged to participate will equal the number who choose not to, relative to the unconstrained program. Therefore, we assume that 126,000 households participate and receive, on average $1,587 per year (1983 dollars).

The increased housing expenditure per household is then the income effect (an average of one to three hundred dollars extra expenditure on housing per year per household), plus the price effect. To estimate the price effect using the extreme example discussed earlier, we assume that 126,000 households participate at all rates of assistance. Estimates are made for average rent payments of 300 and 400 dollars per month, and for elasticity estimates of -0.4, -0.6, and -0.8. To get an idea of the effect on an individual household, we first provide an example of a household with income is $16,000 which pays, prior to assistance, 25% of income as rent ($333 per month), and which has a demand elasticity of -0.6. The implied increase in the quantity of housing as a result of the reduced cost of marginal units of housing is 45%. Monthly rent would rise to $483 (1.45 x 333) so, total assistance would be 0.75 (483 x 12 - 0.25(16,000)) = $1,347. While the move, at first glance, from renting accommodation at $333/month to accommodation at $483/month may seem excessive, note that the out of pocket expense for the household is only $449, or $40 per month.

The design of a constrained housing allowance leaves the total assistance paid to households open-ended. Consider the extreme example mentioned earlier where the housing allowance is designed to finance only increases in housing expenditure. With i) an assistance rate of 90%, ii) initial rents of $400 and iii) a demand elasticity of -0.6, each household would increase its expenditure on rent by $216 (0.9 x 0.6 x $4,000) or $2,592 per year. The housing allowance would be $2,333 per household or $294 million for all 126,000 households per year.

The simulation of a 90% assistance rate that has just been presented serves to illustrate the earlier contention that the same dimensions as an unconstrained housing allowance have substantially different effects when incorporated in an unconstrained allowance. Table 7.4 shows estimates of the effects of a housing allowance on housing expenditures of recipient households under different assumptions about the assistance rate and the elasticity of demand for rental housing. These results need to be put into a perspective. The additional housing expenditure for all households ranges from $357 million (elasticity -0.4 and rate of assistance 0.5). Similarly, the counterpart expenditure on housing allowances ranges from as much as $272 million to as little as $46 million. Still these results must be placed in an appropriate perspective. These estimates of the costs of housing allowances are minimal estimates indicating the expenditures that are required by the fact that households spend more on rent. To this sum must be added the allowances which must be paid to reflect the existing rents paid by eligible households.

4.4 Increased Housing Consumption

The middle estimates of increased dollar expenditure on housing calculated in the last section are about $1,500 per recipient per year, or about four or five times larger than the increase in expenditure for the unconstrained program. In the case of the unconstrained program, the choice of supply elasticity was largely irrelevant since even the smallest estimate produced virtually no (one per cent) price change. In this case, the elasticities are more important.

TABLE 7.4

The Effects on Housing Expenditure and Total Assistance Paid Under Different Housing Allowances

Original Rent	Rent After Allowance	Assistance Paid
I	75% Assistance Rate	
Elasticity -0.4	30% increase in expenditure	
$300/month	to $390/month/household or $136 million/year for all households	$67.50/month or $102 million for all households per year
$400/month	to $520/month/household or $181 million/year for all households	$90/month or $137 million for all households per year
Elasticity -0.6	45% increase in expenditure	
$300/month	to $435/month/household or $204 million/year for all households	$101/month or $153 million for all households per year
$400/month	to $580/month/household or $272 million/year for all households	$135/month or $204 million for all households per year
Elasticity -0.8	60% increase in expenditure	
$300/month	to $480/month/household or $272 million/year for all households	$135/month or $135 million for all households per year
$400/month	to $640/month/household or $363 million/year for all households	$180/month or $272 million for all households per year

Table 7.4 (cont'd)

II	50% Assistance Rate	
Elasticity -0.4	20% increase in expenditure	
$300/month	to $360/month/household or $91 million/year for all households	$30/month or $46 million for all households per year
$400/month	to $480/month/household or $121 million/year for all households	$40/month or $60 million for all households per year
Elasticity -0.6	30% increase in expenditure	
$300/month	to $390/month/household or $136 million/year for all households	$45/month or $68 million for all households per year
$400/month	to $520/month/household or $181 million/year for all households	$60/month or $90 million for all households per year
Elasticity -0.8	40% increase in expenditure	
$300/month	to $420/month/household or $181 million/year for all households	$60/month or $90 million for all households per year
$400/month	to $560/month/household or $242 million/year for all households	$80/month or $121 million for all households per year

NOTE: These estimates measure only the increased assistance caused by increased housing expenditures and not any assistance required by existing levels of rent. Alternatively each household can be assumed to be at the threshold at the introduction of the program.

As well, the assumption regarding financing also becomes more important.

If the program is financed through taxes or non-recipient renter households, their demand for housing expenditure can be expected to fall by between 12 and 38 million dollars. Against this, increased expenditure by recipients can be expected to increase by about 200 million dollars. The net increase is, therefore, between about 160 and 190 million dollars. Using a supply elasticity of zero (no new additions to rental housing due to price increases), a net increase in expenditure of $160 to $190 million implies a 3.5% to 4.3% increase in rental prices with demand elasticity of one and a 4.4% to 5.4% increase with demand elasticity of 0.8.

If a somewhat more elastic supply curve is used, expected price increases diminish quickly: with a supply elasticity of 0.3, the expected price increase falls to 3.5%; with a supply elasticity of 1.3, the price increase is less than 2.5% and with an elasticity of 2.0, the price increase falls to around 1.2%. The increases in the stock of rental housing range from zero (zero supply elasticity) to about 3.5% with a supply elasticity of 2.0. It should be pointed out that these estimates are biased toward producing small quantity changes and large price changes since most estimates of the elasticity of supply are significantly above those used here.(16)

As in the case of the unconstrained program, price effects will not only reduce the increase in housing for the target group households, but will also have an impact on financing households. The maximum impact on financing households in the unconstrained case was about $40 million dollars among the 950,000 non-eligible renter households. Because of the greater number of dollars channelled into housing arising from the constraint that assistance be used for housing, the constrained program has a much larger potential impact. The maximum calculated price impact (4.5%) would cause non-recipient households to increase rent payments by $180 million per year in excess of their tax payments. This amount would be collected by landlords in the form of higher rent under the assumption that the elasticity of supply was zero. With larger elasticities, the increase in price and therefore cost to non-recipients falls very quickly. Even at elasticities of only 2, the cost falls from $180 million per year to about a third of that.

In summary, the housing consumption changes for target households under the constrained program would be significantly larger than those under the unconstrained program. However, the increased expenditure would be more costly to non-recipient renters (beneficial to landlords) and tend to be more beneficial to those households who have more "taste" for housing as opposed to other goods or services. Federal and provincial tax revenues would also be affected since the increased rental payments to landlords would be taxable income.

4.5 Summary of Constrained Demand Program

- same number of eligible and participating households (as unconstrained program) but of different composition; households of low housing consumption and low income would not be eligible for the constrained program since the assistance is based upon actual payments rather than some average level; those who pay less than 25% of income are not eligible, independent of level of income;

- average increase in housing services to target households about fifty per cent, depending upon price impacts. The higher values are more likely, given the small supply responses assumed. Non-recipient households may experience as much as a three and a half per cent reduction in housing consumption (or alternatively, a 4.5% increase in rent).
- increase in total rental housing stock of between zero and 7%; the 7% value calculated on the assumption of infinite supply elasticity; 3.5% increase on the assumption that the elasticity is around 2.0

5.0 Subsidized Supply Program

5.1 Rent Supplement Program

This program is patterned after the Rent Supplement Program (1971) used in Ontario.(17) Landlords sign five year contracts with the Ontario Housing Corporation (OHC) whereby they rent specified units at agreed, below market rents. Tenants are chosen by OHC from public housing waiting lists and rents are geared-to-income. Rents typically run from about 17 to 25 per cent of income although for participants who were recipients of general welfare or family benefit assistance, rent was set at the level of the shelter allowance component of the assistance.

If we assume similar eligibility and participation rates for this program as for the demand side programs (157,000 households eligible, 80% or 126,000 households participating), then average assistance will be the same ($1,587) except for increased administrative costs occasioned by this program.

While dollars of assistance may be the same under this program as under a housing allowance program their value to participating households will be less. The reason is that under this program, tenants have less choice of their accommodation. If a tenant under the demand program wishes to move either because of job opportunities or changing household composition (fewer children requiring access to schools, etc.) then the assistance moves with the household. In the case of a subsidy program such as the rent supplement program, the assistance is attached to the unit, and the number of potential units will necessarily be much smaller. The fact that there will be fewer eligible units also has another dimension in that if the size of household changes such that smaller accommodation is one option, the supply assistance program acts to encourage households to remain in larger units rather than move. In the unconstrained demand assistance program, there are incentives for households to conserve space and quality since the assistance can be used on other goods and services.

Another difference between the demand programs and this supply program relates to the ability of landlords of subsidized units to appropriate some of the assistance, even if there is no change in the level of nominal rent. In the demand program case, landlords who reduce service or upkeep are subject to the loss of their tenants. The constraint on tenants is that moving is not costless so the loss of service must be greater than the cost of the move, appropriately discounted, before a move will be made. In the case of the supply program, where tenants on assistance are known because of the units they occupy, landlords can reduce service etc. by a greater extent since the costs of moving are higher to supply assisted tenants. They must, first, find an empty subsidized unit rather than just an empty unit. The fewer units with appropriate size and locational characteristics means that such tenants will accept a greater amount of reduction of service than will tenants who are assisted by an equal amount of money through a demand side program and, hence, have lower costs of moving.

An additional, although perhaps less important implication is that landlords can act in such a way as to increase rent levels even where the rent levels are ostensibly market level. To ensure that "market" rents are charged, suppose that landlords are only eligible to be subsidized for given units when those units are in the same building as unsubsidized units and nominal rents are the same. This rule would reduce the extent to which landlords could reduce service to tenants who have high costs of moving since some (or perhaps all) of the reduced service would be experienced by unsubsidized tenants who would be more likely to move. However, the rule also allows the landlord a way in which to charge higher rents for all units in spite of the apparent check for "market" level rents. This ability comes from the fact that the rent charged for any unit affects the vacancy rate in a positive way -- higher rents are associated with higher vacancy rates. Unless the government is willing to pay a subsidy for units which are empty, a non-zero waiting list will ensure that subsidized units are always full. By increasing rent levels for all units, and therefore apparently charging "market" rents for the subsidized units, the landlord will create some vacancies in the unsubsidized units. If the increase in rent from subsidized units and the occupied unsubsidized units is greater than the cost of the higher vacancy rate of unsubsidized units, the landlord will profit from such activity. For example, if raising the rent by 5% increases vacancies by 10%, then the rent increase will increase revenue as long as more than about half (53%) of the units are subsidized. If a five per cent increase in rents causes a twenty per cent increase in vacancies of unsubsidized units, then such an increase will be profitable for the landlord as long as about 76% of the units are subsidized.(18)

This activity by landlords will produce the appearance that subsidized units are being rented for the same rent as unsubsidized units. However, while this is true for a given apartment building, this does not imply that the units are collecting market rents -- if the building had no subsidized units, the vacancy rates consistent with profit maximization by the landlord would be such that a lower rent for all units would be charged. Effectively, the rule reduces the cost of raising rents (increased vacancies) and hence landlords will charge higher rents. The illusion that rents are "market" and the same for subsidized and unsubsidized units is maintained, however.

5.2 Summary of Impact of Rent Supplement Program

- If costs of administration were near zero, and the 200 million dollar per year budget is maintained, then this program would assist the same households as the constrained demand program, and would assist them to the same extent;
- Administration costs will likely be higher, however, since the administering agency must be involved in contracting with landlords and must also assign tenants to subsidized units.
- Tenants will value the assistance less since their choice of location and other characteristics is limited.
- Tenants will also value the assistance less than demand assistance because of the reduced mobility provided by a scheme which subsidizes rental units rather than households.
- Rents for constant quality units will be higher due to landlords reducing service for tenants with higher costs of moving (those in subsidized units), and landlords accepting higher vacancy rates in unsubsidized units in order to charge higher nominal rents to all tenants.

6.0 Public Housing

6.1 The Program

For each program discussed so far, annual expenditure was kept at 200 million dollars. In the case of public housing, initial capital expenditures must be translated to annual expenditure through an interest rate. Assuming an interest rate of 10%, 1.5 billion dollars would translate into 150 million dollars per year which would allow for 50 million dollars per year for depreciation and other expenses. These numbers would imply that 30,000 units costing $50,000 in capital expense would have market rents in the neighbourhood of $550 per month. Assuming such a public housing program were free of administrative costs, the subsidy per household for the 30,000 units would then be about $6,600 per year. If the subsidy assistance were reduced to the same level as the demand programs ($1,587), then a public housing program which was not more costly in building or operating rental units than private market agents, could produce about 126,000 units with market rents of $6,600 and subsidies of $1,587 per year per unit. (126,000 units at $47,500/unit approximately equals $6 billion capital or $600 million annual plus $200 million for operating and replacement; $600 million would be the rent collected, $200 million would be the annual subsidy at about $1,587 per household.)

These numbers are the same as for the demand program because we have assumed that public housing would be operated in the same way as would private rental units. We have also assumed that the administration costs are zero for the public agency and building and upkeep costs are identical.

A major difference between public housing and a housing allowance arises from the necessity to finance and construct housing in order to operate a public housing program. A housing allowance can be implemented immediately once the decision has been made to spend the annual sum. In contrast, a public housing program requires first the expenditure of a much larger capital sum on the supply of public housing. Though this capital sum would be self-financing except for the annual subsidy, such an expansion of public housing would take a long time to implement even under the most favourable circumstances. In practice, a greater obstacle results from the reluctance of governments to commit the capital required.

6.2 Differences in Costs

The evidence over a wide range of publicly and privately produced goods and services suggests that public supply is more costly than private supply. Estimates for Canada suggest that public housing may be up to 60% more expensive than similar private rental housing.(19)

Evidence from various sources is broadly consistent with the contention that income transfer schemes, especially those involving in-kind transfers, are more expensive when public production is involved. Browning and Johnson (1982) estimate that the transfer of marginal dollars may cost more than $10, and Sonstelie (1982) estimated that private schools were only 37% of the cost of public schools for quality constant education. In airline operations, Davies (1971) found that the public airline in Australia was significantly more costly on identical routes than the private airlines.

To estimate the number of units which can be supplied at an annual cost of $200 million, we take a range of increased costs - 10%, 35%, and 60%. The number of units which would have average market rents of $550 would fall from 126,000 to 114,500, 93,300 and 78,750 respectively.

6.3 Recipient Households

If households are eligible on the basis of income, only if public production and operation had the same costs as private would households under 1.5 RLIC be eligible for public housing. As the differential in costs rises, the income cut-off would fall. Even if public costs were only 10% higher, the income cut-off would fall to a level only slightly above RLIC and at 35%, the income cut-off would be about 10% below the RLIC level. At 60%, recipients would have to have income levels less than 70% of RLIC.

6.4 Value to Recipients

As in the case of the supply program where housing agencies place tenants, the value of the public housing program to tenants is somewhat reduced because of the reduced choice in initial accommodations (location, size, etc.,) and because of the reduced mobility implied by such programs. Unless the government were willing to hold a large number of empty rental units in inventory, and this would reduce the number of recipients for any given amount of expenditure, households would experience increased costs of moving relative to a plan which allowed them to choose their accommodations from the private market as would be the case of a demand program. If, on the other hand, and as seems most likely from experience, there is a waiting list to be allocated public housing, then households whose needs change because of children leaving, school needs changing, etc., would be less likely to move, given the extra costs of finding, or waiting to find suitable accommodation. In effect, this means that the stock of housing in terms of rental units will be less valuable since at least some of these households will be living in accommodations which are larger or smaller than they would choose under a less restrictive but equally costly plan. Another reason for suggesting that recipients will value public housing at less than cost is detailed by Steele (1985a) who notes that "ghetto-ization" of low income households reduces the value for recipients of public housing.

6.5 Increased Numbers of Rental Units

While the number of public housing units would increase, given the above assumptions, by between 78 and 114 thousand units, the net addition to the stock of rental units will be less than that and could be zero. As new stocks of rental housing are opened up, rental prices will fall (or vacancies rise in the immediate period) and, hence, private resources will be shifted out of the rental market.

Using estimates of supply response which are on the very low end of those available from studies in the U.S. and Canada and, hence, estimates which bias the amount of net addition to housing stocks upward, the expected net additions to housing are as follows:

i) assuming a gross increase of 114,500 units, and demand elasticity of 0.5:

net increase of 47,250 (supply elasticity: 0.7)
38,850 (supply elasticity: 1.0)
30,450 (supply elasticity: 1.3)

These increases would imply reductions in average rent levels of, from about 11% for the largest increase in quantity to 7% for the smallest.

ii) assuming gross increase of 93,300 units, and demand elasticity of 0.5:

net increase of 37,800 (supply elasticity: 0.7)
31,500 (supply elasticity: 1.0)
25,200 (supply elasticity: 1.3)

The rent reduction expected is approximately 8% for the largest increase in quantity and 6% for the smallest.

iii) assuming a gross increase of 78,750 units, and demand elasticity of 0.5:

net increase of 32,550 (supply elasticity: 0.7)
27,300 (supply elasticity: 1.0)
21,000 (supply elasticity: 1.3)

These net increases imply a rent reduction between 5 and 7.5%.

6.6 Summary of Impacts

Under the most optimistic assumptions, including small differentials in costs between public and private costs of supply and administration, and very low estimates of supply responsiveness, a public housing program of $200 million per year can be expected to:

- increase the net stock of housing by, at most, about 47,000 units
- only households with incomes marginally above RLIC would be recipients of assistance
- while other rents would fall between 7 and 11% and would therefore be beneficial to all households with incomes above the eligibility cut-off, it also implies a capital loss to owners of rental households in the neighbourhood of 3 billion dollars (20) ($4.4 billion at 11% reduction in rent). The public

housing program would, therefore, be highly beneficial to higher income renters who did not own rental accommodation. This would also have non-trivial tax implications since the gain to non-owners would be non-taxable while the loss to owners would be subject to tax reductions.

If somewhat less optimistic assumptions are used, then the number of units of net new rental accommodation would fall to about 21,000 (gross 78,750), implying that only households with incomes around the RLIC level would be eligible. Moreover, rent reductions for other tenants (and losses to owners of rental units) would be smaller, at about 5-7.5% of rent or about $2.2 billion to $3.4 billion.

7.0 Summary Comparisons

In this section, we discuss each policy alternative in relation to three basic issues: first, to which households is the assistance provided? second, how much income, in dollars or in kind, is transferred to which households? and finally, what is the change in the stock of housing, both that occupied by the target group of households and others? Table 7.5, at the end of this chapter, restates the main results.

7.1 Eligibility of Households and Distribution of Assistance Among Them

a) Unconstrained demand program

About 126,000 households with incomes below 1.5 RLIC would be assisted according to income, household size, and average housing cost in their location. Assistance which would average about $1,587 (1983) per household, is independent of actual rental costs and the program is neutral with respect to living in high or low rent areas, that is, there is no incentive for recipients to move to higher or lower rent areas.

b) Constrained demand program

The number of recipients would be smaller and the size of assistance would be somewhat larger in the case of the unconstrained program. A small number of households which would be eligible under the unconstrained program would not be eligible because of the requirement that a minimum 25% of income be spent on rent. The distribution of benefits would be different because assistance is determined, in part, by actual rent payments. Households, therefore, have incentives to increase housing expenditure and move to higher rent areas. Households which choose more expensive accommodation, for given size and income, are more highly assisted than are households which choose less expensive accommodation. The incentive for increased housing expenditure means that fewer households can be assisted for any overall level of assistance.

c) Supply program

The supply program would support somewhat fewer households than a constrained housing allowance. The main difference between the two programs consists of the limitation of renters' choices to the housing made available under the program. This difference, by limiting the range of choice for participating families, may cause upward pressure on rents of assisted units. To the extent that it occurs, the increased costs of assisting the typical household would mean that fewer households can be assisted.

d) Public housing program

If the extreme assumption is made that the administration and operation of public housing is no more expensive than private housing, the recipients of assistance under public housing will be the same as those under the constrained demand program, given that public placement agencies use income and family size as the criterion. However, to the extent that public provision implies any extra costs, the number of recipients or average level of assistance will fall proportionately. Empirical estimates of the extra costs involved run to 60%, in which case 60% fewer households (or 60% reduced assistance, or a combination) will receive assistance.

7.2 Income Transfers to Low Income and Other Households

For all policy alternatives, the assumption that annual expenditure is constant at $200 million means that there will be, at least, a transfer from taxpayers to recipients of some portion of that 200 million dollars (some might be 'redirected' through price increases or leaked through higher costs of administration or operation in the case of supply subsidies or public housing). This section summarizes those effects which are implicit in the programs rather than designed into them.

a) Unconstrained demand program

If this program is financed by households which have the same tastes in housing as recipients, there will be no net change in demand for housing and hence no price effects. The total transfer in dollar terms is, therefore, the 200 million dollar cost of the program. At the other extreme, if the financing households do not reduce their expenditures, there will be a net increase of 12 to 38 million dollars of demand from recipient households and depending upon the supply response, prices would rise from zero to just over one per cent. This maximum price change implies a transfer of about $54 million from all tenants to landlords. Assuming that the average rent for recipient households is 75% of non-recipient households, this means that about 6% of the transfer is from recipient households. There is a small impact on federal and provincial taxes since the extra $54 million dollars is taxable income.

b) Constrained demand program

The effects of a constrained demand program, like those of an unconstrained program, depend on the supply conditions in the housing market. A constrained demand program causes a larger increase in the demand of housing than does an unconstrained program. Under the least favourable conditions, the increase in the demand for housing implies that rents will increase by as much as 4.5%, depending on the responsiveness of the demand for and supply of housing. The 4.5% increase in rent causes a transfer of $180 million annuall from tenants to landlords with a concomitant increase in the tax revenues of the federal and provincial governments. Under the most favourable conditions, the whole of the transfer remains with the assisted households.

c) Supply program

A rent supplement program has essentially the same effects on rent levels as a constrained demand program. In the least favourable case where the supply of housing is inelastic, rents rise by as much as 4.5%. In this case, most of the $200 million subsidy will be collected by landlords. Nevertheless, recipient households still gain because the increase in rents only offsets a small proportion (approximately one quarter) of their assistance. Other tenants bear much of the costs of higher rents. Governments, on the other hand, gain some of the benefits through higher tax revenues. If the supply of rental housing is perfectly elastic, the subsidy will be seen entirely as lower rents for the assisted households.

d) Public housing

Assuming that the public housing program is not more costly than private operators' production and operation of housing, the transfers under this program will be similar to those under the constrained demand program. To the extent that public housing costs are higher, benefits are directed away from the target group of households toward suppliers of the housing and operating services.

Because of the estimated reduction in market rents due to this program which are in the 5 to 11 per cent range, there will be a transfer away from landlords towards unsubsidized tenants in the area of 220 to 440 million dollars per year. The extra housing services per dollar will be untaxed, of course, but the reduction in landlords' incomes will result in lower taxable income of the 220 to 440 million dollars per year, with resultant effects on federal and provincial revenues.

7.3 Increased Housing Consumption

a) Unconstrained demand program

Given the small estimated income elasticity of demand for housing, the annual expenditure of 200 million dollars only represents from 12 to 38 million dollars of extra housing for recipient households. With price increase estimates at a maximum of one per cent, this implies an increase of average housing services to low income households of up to about 13%. The increase in price and assumed constancy of expenditure by financing households implies that their consumption falls by up to one per cent. The net addition to the stock of housing under this program is about one per cent.

b) Constrained demand program

The constrained program reduces the effective cost of additional units of housing services to low income households by the proportion by which assistance makes up the gap between 25% of income and housing expenditure up to 90%. This results in a large substitution into expenditure on housing by this group of households, estimated to be in the neighbourhood of 30%. The price effect implies that the 30%

increase in expenditure results in about a 26% increase in the consumption of the quantity (or quality) of housing services by assisted households. Financing households, on the other hand, reduce their consumption of housing up to 3%. The net addition to the stock of housing under this program is from zero to seven per cent, depending upon the estimated supply response to the increased expenditure on housing.

c) Supply program

As in the other dimensions reviewed up to this point, the effects of the supply program are similar to the unconstrained demand program. In the least favourable case, the assisted households face rents that are higher by 4.5%. Still they experience an increase of about 26% in the quantity or quality of their housing. Under the most favourable conditions, all of the 30% increase in rental expenditure is reflected in improved housing.

d) Public housing

Of the (maximum) 120,000 rental units which would be produced, assuming no differential costs between public and private suppliers, only between 20,000 and 45,000 should constitute a net addition to the stock of rental housing. The subsequent reduction in rent would result in a reduction in private supply by between 75,000 to 100,000 units.

TABLE 7.5

Summary Comparisons, Impacts Ranked by Program, Eligibility of Households and Distribution of Benefits

Program	Impacts
Unconstrained Demand	- 126,000 households, income below 1.5 RLIC
Constrained Demand	- somewhat less than 126,000 households but the income cut-off would be below the 1.5 RLIC
General Supply	- up to 126,000 units, depending on the level of administrative costs and added pressure on rents
Public Housing	- between 78 and 114,000 households with income cut-off levels between about 0.9 RLIC and just over RLIC
Income Transfers to Low Income and Other Households	
Unconstrained Demand	- approximately $1,450 per year average assistance, dependent only upon income level
Constrained Demand	- average payment as in the unconstrained program but will be directed to those households which choose relatively more expensive accommodation
General Supply	- in the directed program, the assistance will be less than the demand programs because of added costs of administration and the increased costs of tenants due to their restricted mobility
Public Housing	- assumed $1,450 per year average assistance but to fewer households (see Distribution, above)
Increased Housing Consumption	
Unconstrained Demand	- between 9% and 13% increase in housing expenditure per recipient household
Constrained Demand	- between 37% and 74% increase in housing expenditure per recipient household

Table 7.5 (cont'd)

General Supply	- approximately 35% average increase in consumption for recipient households
Public Housing	- similar increase to the supply program except that fewer households will be recipients

Notes to Chapter 7

(1) Some statistics used to estimate the number of eligible households etc. are drawn from samples using a thirty per cent of income criterion.

(2) Steele 1985a. Table J1.

(3) Steele, 1985a, Table 13.

(4) Steele, 1985a, Table 13.

(5) Steele, 1985a, Table 15.

(6) Steele, 1985a, Table 14.

(7) Straszheim, 1981, Table 3.

(8) These incomes and rent figures are adjusted from Miron and Cullingworth (1983), Table 7.9. Changes in prices and income and income distribution are those from "Income Distribution by Size, in Canada", Statistics Canada SC 13-207, 1984. The income levels for the three households are near RLIC for single persons in 30-500,000 population centres (household 1), two person households in centres over 500,000 population (household 2), and a three person household in centres over 500,000 population (household 3).

(9) For incomes around $10,000 per year, this would imply income elasticities of the values, 0.06 to 0.19. For enrolled renters, Mills and Sullivan (1981) estimated income elasticities of about 0.25. Haunshek & Quigley (1979) estimated numbers of 0.14 to 0.24 (Steele, 1985a, p. 131). These numbers imply that lower income households will spend proportionately more on housing than relatively higher income households for given increases in income.

(10) That is, with assistance of $3,024 (see discussion following Table 7.3), increased expenditures on housing would range from a low of $180 to a high of $575.

(11) With 1,100,000 rental households paying an average of $500 per month, the additional 38 million dollars represents 0.7 of one per cent increase in expenditure on housing. Since we assume no supply response, this is a 0.8 of one per cent increase in rental prices. If a lower average rental figure of $400 per month is assumed, the increase in price goes up to one per cent.

(12) The 10% is calculated on the basis that average rent of recipient households is about $300 per month. Even at an average rent of $200, there is still only a 13% increase and at $400, the increase would fall to 6.5%.

(13) A technical discussion of this factor can be found in Appendix 2 to this chapter.

(14) This lack of realism can be illustrated by the fact that the elimination of the static costs of the program requires that the threshold rent be different for each household at the present level of its rental expenditures.

(15) Steele, 1985, Table J1.

(16) Steele (1985a) states "The evidence...suggests that the response of the price of housing service to housing allowance programs is so small as to be undetectable. This is true in the U.S....[and] Canadian sites of housing allowance programs." (p. 136) See also Appendix 1 to this Chapter.

(17) Fallis, (1980), p. 144.

(18) Assuming an original occupancy of 100%, average rent is $pR + (1-p)R$, or just R, where R is the rent paid, and p is the proportion of units rented on a subsidized basis. After an x per cent rent increase and a y per cent occupancy decrease in the unsubsidized units, average rent is $pR(1 + x/100) + (1-p)R(1 + x/100)(1 - x/100)$. The change in average rent is therefore: $pR(x/100) - (1-p)R(x/100 - x/100 + xy/10{,}000)$. Setting $x=5$ and $y=10$, average rent will rise if at least 53% of units are rented on a subsidized basis. If $x=5$ and $y=20$, then at least 76% of units must be rented on a subsidized basis.

(19) MacMillan and Nickel (1974) suggest that a 1.6 million dollar expenditure would have cost about $1 million if produced by private market agents.

(20) 738,000 rental units at (modest) $500 per month less 7% of rent = $3.1 billion loss at 10%.

Appendix 1 to Chapter 7: The Elasticity of Supply of Rental Housing

by David Griffiths

1.0 Introduction

This section contains a selective review of the literature pertaining to the supply response of rental accommodation with respect to price. The conclusions to be drawn with respect to the effects of housing allowance and other housing programs depend basically on the supply response to a shift in demand for rental accommodation which occurs as a result of the Housing Allowance program.

In turn, conjecture regarding the price or rent elasticity of supply of rental accommodation depends upon what is believed regarding the structure of the submarkets of the metropolitan area housing market. It is useful to classify potential supply response into two conceptual extremes:

Case I: Elastic response with respect to own price; characterized by very few barriers to conversion of housing units from one level of service to another; few barriers to households moving within an area; cross elasticities of demand between areas is high. In such circumstances, changing demand in any one sector will have negligible impact on overall rents.

Case II: Inelastic response with respect to own price; characterized by highly inflexible market; increasing marginal costs; zoning laws and other barriers to preventing conversion of housing units from one level of service to another. In such circumstances increased demand for rental accommodation results in windfall profits for landlords since the price of new and existing rental units is increased. Consequently any benefit to income recipients could be entirely dissipated in rental increases.

Having established the desirability of obtaining an estimate of supply response, it is necessary to examine the evolution of the literature that has explored this question. Table 1 gives an indication, in chronological order, of results derived from available studies on U.S. data for both rental and non-rental accommodation. Cursory examination of this table suggests that there is no widespread agreement regarding supply response. This may be the result of differences in the structure of markets, both spatially and in terms of different time periods studied, and possibly due to differences in methodologies employed in measuring this response which reflect the author's purpose. Consequently, in Section 2, we shall examine the evidence for and against the contention that the supply of rental housing is highly price elastic. The evidence is drawn from three types of studies: i) long run supply analysis, ii) short run supply analysis and iii) simulation studies.

2.0 Chronology of Literature on Rental and General Housing Supply Response

2.1 The long run supply response

A classic early reference to the question of supply response of U.S. general non-farm housing to changes in demand can be found in Muth (1960), where evidence is presented that suggests there is a high degree of mobility of resources into the new home building industry in both the

TABLE 1

Summary Tables of Housing Market Studies

Study	Supply	Comments	Housing Category
Rosen and Smith (1983)	"rental price changes significantly affected by excess supply demand"	17 U.S. cities pooled x-section time series. Short run supply	Renter
Rydell (1980)	"highly elastic"	Housing allowance program (HUS) U.S. data	Renter
Follain (1978)	"highly elastic"	long run supply OLS and TSLS	General new housing units
Mason (1979)	"significant positive relationship between residential housing and its price"	short run supply I.V. extinction technique	General new housing units
Kain and Apgar (1976)	full scale housing allowance program would cause price increases of around 10%	NBER; simulations for Pittsburg & Chicago	General existing housing
de Leeuw and Struyk (1975)	0.4 - 1.1	Urban Institute large scale simulation model, U.S. data	elasticity of supply of existing general housing units
Grieson (1973)	+2.2	modified version of specification used by de Leeuw & Ekanem (1971) (2)	Renter
Grieson (1971)	2.36 to 5.0		General new housing units

Table 1 (cont'd)

Study	Supply	Comments	Housing Category
de Leeuw and Ekanem (1971)	0.1 to 0.4 (a) + 0.7	(a) long run elasticity w.r.t. rental price for low rental group (1)	Renter
de Leeuw (1971)	N.A.	X-Section review; elasticity w.r.t. quantity of rental demand	Renter
Muth (1968)	"highly elastic"		general new housing units
Muth (1960)	"highly elastic"	long run elasticity w.r.t. quantity of rental supply and demand	general non-farm housing

NOTES:

(1) For medium and high rental groups, as defined in the BLS Study, the elasticities of supply of housing services with respect to rent per unit of service are 0.5 and 0.3 respectively.

(2) In the Grieson study, the supply elasticities in (1) are found to be 1.8 and 0.37, respectively.

short and long run. For the period 1915-34, Muth presents regressions which show no relation exists between the quantity of new construction and other variables in the supply function. A second regression indicates that much of the variation in house price can be explained by other variables in the supply function, such as wages, etc., but the quantity of new construction contributes nothing to the explanation. This evidence suggests that "shift" factors which determine the location of the supply function are more important determinants of housing price than are "output" factors, which determine its elasticity. Muth therefore concludes that it is reasonable to treat this sector of the housing market as approximately perfectly elastic in supply response. Similar evidence is presented in Muth (1968). Furthermore, Follain (1979) presents more recent evidence covering the period 1947-75 (for the U.S.), which corroborates the contention that the supply of new housing construction is price elastic in the long run.

De Leeuw and Ekanem (1971), arguing that Muth's (1968) evidence is incomplete because it ignores the cost of operating inputs and maintenance of existing capital stock, present evidence which suggests that the supply response of rental accommodation may not be as elastic as had been thought. They make the distinction between several possible sources of rising supply price for housing services, using measures of rising price of capital and operating inputs, combined with the idea that there may be two kinds of diseconomies of scale: those that result from maintaining the existing stock of rental accommodations and second, those that result from the production of services from a given stock.

Through a technique which involves an "errors in variables" specification, they test for shift versus elasticity factors in the determination of rental prices. Stated briefly, they argue that the null hypothesis of a perfectly elastic supply function should be rejected if the coefficient of income in a reduced form regression for the price of rental housing is greater than zero. They find that both shift and elasticity factors are significant, although they point out that there may be problems with errors of measurement which may cause systematic downward bias of the rental elasticity estimate. They do conclude, however, that housing assistance may drive up rents.(1) Grieson (1973) in making a minor change to the specification in the same estimating equation, demonstrates the sensitivity of their results to *a priori* specification. It is shown that with a minor change, the supply elasticity of housing services with respect to price is much greater. This is also supported by an earlier study in which Grieson (1971) computes supply elasticity of 2.36 to 5.00 using a different technique.

2.2 Short Run Studies of the Effects of Vacancy Rates

Short run effects: Although not all researchers might agree, we have chosen to group the body of research on vacancy rates into this category. This is because in the long run new construction and removals limit the variation in vacancy rates. Traditional theory, which asserts that changes in rents should vary inversely with vacancy rates within a critical zone of occupancy, has both supporting and non-supporting empirical evidence in the literature.

Recent supporting evidence can be found in Rosen and Smith (1983) who suggest that rental price changes are significantly affected by excess supply or demand in the rental market. In a study that utilizes pooled cross section - time series data for seventeen U.S. cities, they conclude that a close relationship exists between variations in rental prices and deviations of actual vacancy rates from normal vacancy rates. In contrast, however, Eubank and Sirmans (1979) find that vacancy rates were less important than changes in operating expenses in explaining rental price changes. Furthermore, de Leeuw and Ekanem (1971) find that although a simple negative correlation exists between rental price and vacancy rates, when other cost factors of a long run nature are included in the specification, the rental/vacancy relation breaks down. It seemed reasonable as a first approximation to suggest that the short run/long run taxonomy we adopt reconciles the differences in the research findings of the recent literature with respect to vacancy rates versus cost factors in the determination of rental price.

2.3 Simulation Models

Two U.S. simulation models suggest that housing (not rental) prices will increase with a housing allowance program. Yet simulation models by their very nature indicate only the researcher's judgement of the size of the critical response. These are the Urban Institute [de Leeuw and Struyk (1975)], and NBER models [Kain and Apgar (1976)]. However, Rydell (1980) compares the Urban Institute simulation with an ex post simulation which takes into account actual supply response, finding that repair of substandard housing, supply response, and occupancy rate adjustment reduce potential price increases by 97%.

It is useful, in light of these rather varied empirical findings, to examine the differences between expected and actual effects of housing allowance programs. Barnett (1979) conducts such an exercise. There are four main elements in the area of expected effects.

1) "Analysts usually assumed in predicting price effects that the short run supply of housing was quite inelastic." If so, increased spending for housing by allowance recipients would be dissipated by rent increases, and landlords would reap windfall profits (p. 281).

2) If allowances were not earmarked, most of the money would be spent on other goods because most poor households lived in good quality apartments, but paid a high proportion of their income in rent.

3) Earmarking may reduce the supply elasticity by shrinking the supply of housing that allowance recipients could occupy (It might also decrease the demand for lowest quality dwellings).

4) Housing markets characterised by high vacancy rates would be expected to have a more elastic short run supply response.

However, Barnett suggests there was virtually no effect on rental prices. These findings were the result of:

1) Market conditions seemed to have little input on rents.
2) Cost of upgrading was relatively small.

3) Housing expenditures do not increase much with enrolment.
4) Demand increases slowly as a result of gradual enrolment in programs.

3.0 Conclusions

1. It is evident that there is little in the way of convincing evidence from Canadian data on which to form an opinion regarding supply response, because there is virtually no published material that explicitly explores this question.

2. Those studies of the U.S. housing and rental markets which examine supply response can be divided into short run (vacancy rate) studies and long run (cost factor) research.

3. Ex-post evidence from actual experience seems to indicate that expected supply responsiveness had previously been underestimated, with consequent over estimates of rental price impacts that would result from rental allowance programs.

Notes to Appendix 1

(1) Despite the fact that their actual elasticity estimates are probably biased downward (see also Grieson [1973]), they do conduct some interesting correlations based upon these numbers. They consider the effect of a demand subsidy specifically earmarked for housing versus a general income subsidy. Assuming an earmarked subsidy raises average income by 10 percent, then if low income families spend 25 percent of income on housing, recipients' housing demand would increase by 40 percent ($s = 10/25 = 40\%$) for the earmarked program. The rental elasticity with respect to income of 0.14 to 0.4 gives an increase in rents of 4 to 16 percent for the earmarked program, 1 to 4 percent for the non earmarked program. Again it should be stressed that these figures are probably upper limits to actual elasticities.

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Appendix 2 to Chapter 7: Estimates of the Costs of a Constrained Housing Allowance: The Effects of Income Dispersion

The estimation of the costs of a constrained housing allowance involves two steps: i) the estimation of the costs of assistance to households on the basis of their incomes and expenditures prior to the housing allowance and ii) the additional costs resulting from their changed behaviour in response to the housing allowance. This appendix considers this first factor in some detail.

The first element of the costs of a housing allowance, the costs of assistance to households on the basis of their incomes and expenditures prior to the allowance, corresponds to a static estimate of the cost of the program. A useful benchmark in making a static estimate is the cost of an unconstrained allowance.

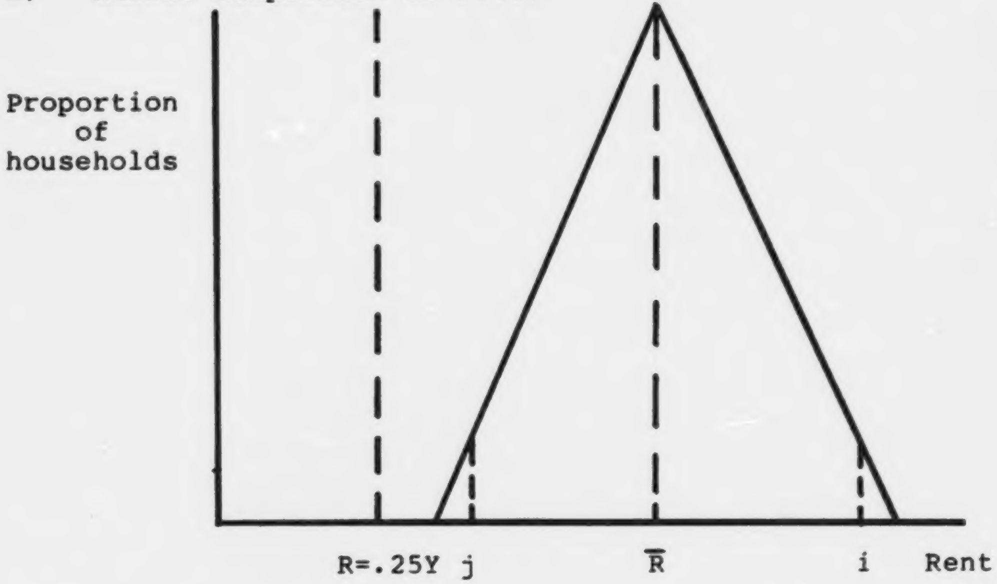
An unconstrained allowance, it will be recalled, pays assistance according to the differenece between some average rent level and a specified proportion of the income of the household. As an example consider Figure 7.1, which shows the distribution of rents paid by a group of households under two assumptions with respect to the distribution of rents paid. In each case, an unconstrained housing allowance pays a portion of the sum $(\bar{R} - .25Y)$ to each of the households where $\bar{R}$ is the average rent payment. The total payment for n households would then be $n(\bar{R} - .25Y)$.

The cost of an constrained allowance need not be the same as the cost of an unconstrained allowance. The difference depends on the dispersion of rental payments among households. To see this effect, consider two households, i

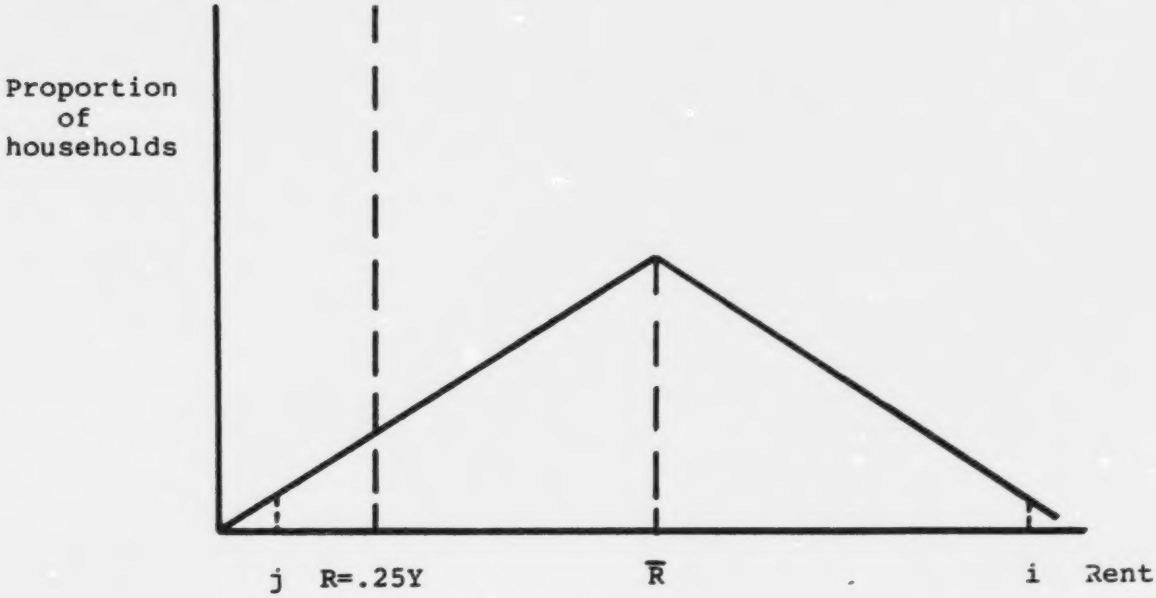
FIGURE 7.1

Rent Payment by Households, Given Income:
Mean Rent Above Threshold

a) Narrow dispersion of rents


Proportion of households
R=.25Y
j
$\overline{R}$
i
Rent

b) Wide dispersion of rents


Proportion of households
j
R=.25Y
$\overline{R}$
i
Rent

and j, one which spends more than $\bar{R}$ for rent and the other pays less than $\bar{R}$ for rent.

The move from an unconstrained allowance to a constrained allowance requires the replacement of average rent by actual rent paid by each household. Households spending more than $\bar{R}$ gain greater assistance under the constrained allowance whereas households spending less than $\bar{R}$ gain less assistance. If these differences in payments cancel out, the static estimates for the constrained program would be identical to the costs of an unconstrained program. On the other hand, if the dispersion of rents is sufficiently great, the household spending the least on rent may fall below the threshold for assistance. Unless there were a maximum to assistance, the reduced payments to the one household will not offset the increased payment to the other household. Whether the two effects cancel depends on the dispersion of the rents paid.

Figure 7.1a shows a narrow dispersion of rents among households. Here the allowance paid to individual i will be based on $(1.25\bar{R} - .25Y)$ because i pays 25 per cent more on rent than the average household. On the other hand, the allowance paid to household j equals $(0.75\bar{R} - .25Y)$ because j pays 25 per cent less rent than the average household. Note that the additional payment to i under the constrained plan just offsets the reduced payment to j. The total payment to i and j together just equals the combined payment under the constrained program.

The effects of dispersion differ as the degree of dispersion increases. Panel b) of figure 7.1 shows a circumstance where the dispersion of rents is so great that individual j lies below the threshold rent level, given income, to qualify for assistance. Household i's rent payment is sufficiently above $\bar{R}$ that it would take negative assistance to j in order to offset the greater assistance to i. However, the assistance to j is limited to zero or above.

A final case to be considered is presented in figure 7.2. Here the average rent paid by households of this income group falls short of the threshold proportion for assistance. Under an unconstrained housing allowance, households from this income group would not receive any assistance. As can be seen from panel a) of figure 7.2, these households as a group do not receive any assistance because all have rent-to-income levels below the threshold. Panel b) shows a greater dispersion of rent-to-income ratios for this group. As can be seen, this greater dispersion brings some households above the threshold for assistance.

This analysis of the effects of dispersion of rent-to-income levels on eligibility of households for assistance under a constrained housing allowance has important implications for calculating the costs of such a program. The cost of a comparable unconstrained program can serve as a base for static estimates only under quite stringent conditions:

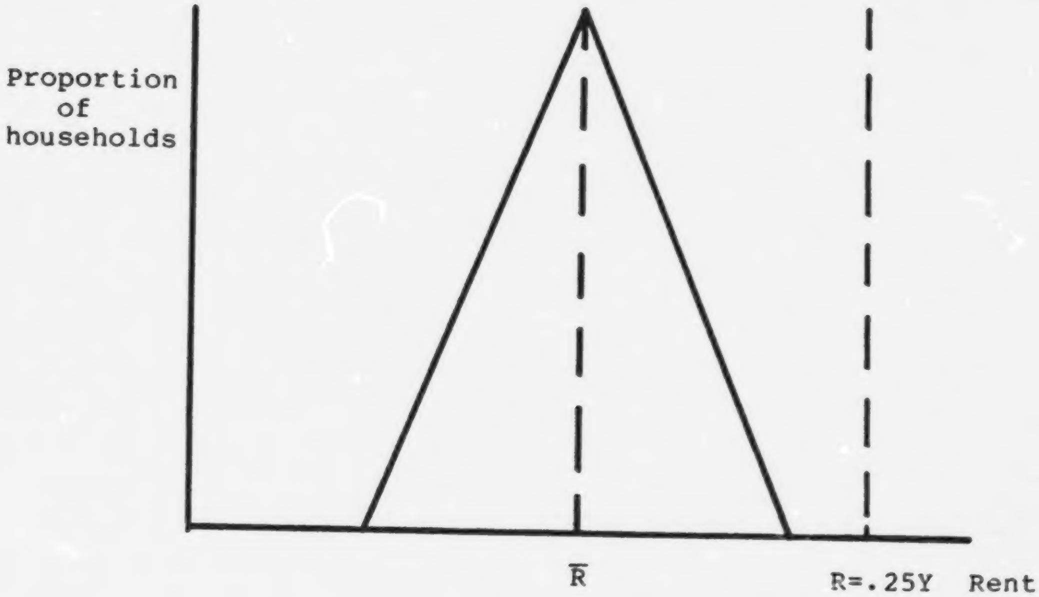
i) none of the households in income groups receiving assistance under the unconstrained program can have rents below the threshold level for support.

ii) none of the households in income groups which do not receive assistance under the unconstrained programs can have rents above the support threshold under the constrained program.

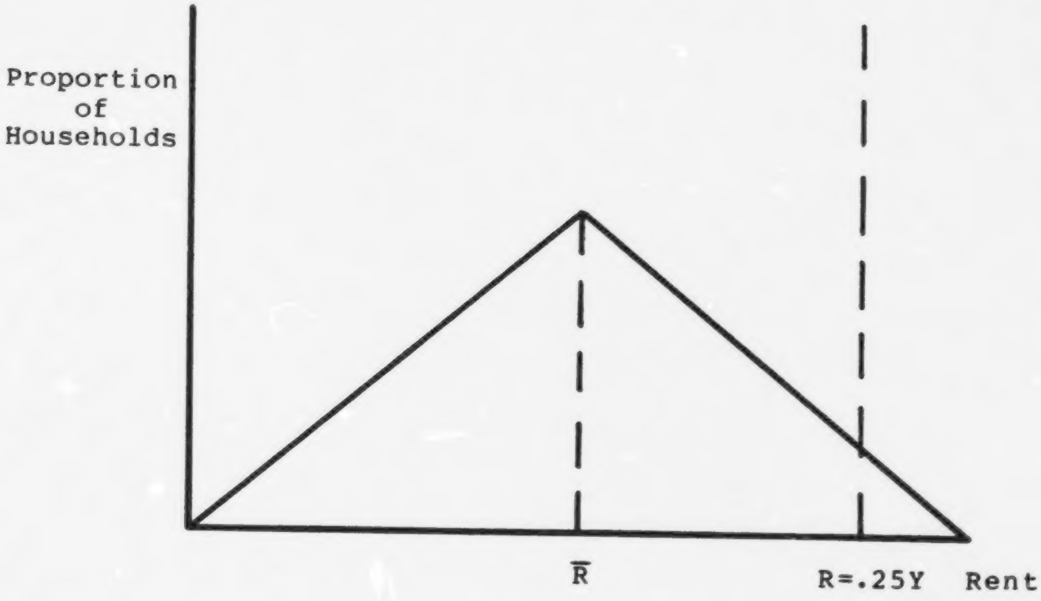
Figure 7.2

Rent Payments by Households, Given Income:
Mean RentBelow Threshold

a) Narrow dispersion of rents



b) Wide dispersion of rents



If either of these conditions are not fulfilled, a static estimate of the costs of a constrained program must exceed the costs of an unconstrained program with the same support rate and threshold rent for eligibility.

CHAPTER 8: CONCLUSIONS

1.0 The Role of Complementary Policies

This study, as stated in its introduction, has examined rental housing policies that are complementary to rent regulation. These policies consist of those that can be used in conjunction with rent regulation to achieve the objectives of housing policy. The introduction also suggested the reason for such a study. Any policy has strengths and weaknesses with respect to the different aspects of its performance. A policy should be deployed toward those objectives for which it has a comparative advantage. While a policy may be superior with respect to some objectives, it may perform poorly with respect to other dimensions. Indeed, the costs of its superior performance with respect to one policy objective may be the creation of harmful side-effects in others. Given the mosaic of goals (Chapter 3) toward which housing policy is directed, it is not possible for them to be achieved by a single policy instrument.

These rather obvious observations have profound implications for the conduct of housing policy or any other type of economic or social policy. The various policies available to government should be arranged together in such a way that its chosen policy objectives be attained at least cost.

2.0 The Interrelation Between Budgetary and Non-budgetary Policy

The policies assessed in this study share a common characteristic that they impose budgetary costs in order to realize their objectives. Some are expenditure policies which require governments to obtain funds to carry out the expenditures. Others work through tax incentives which require governments to forego revenues, thereby inducing behaviour by taxpayers which contributes to the policy objectives. In addition, budgetary programs can impose costs upon households in ways other than through the need to finance government's expenditures or lost revenues. For example, as discussed earlier, housing allowances could under unfavourable conditions impose costs on non-target households by placing upward pressure on the level of market rents.

Budgetary programs may be compared to non-budgetary programs. Non-budgetary programs are not costless. Rather, they impose burdens upon market participants, primarily tenants and landlords. Much of the apparent appeal of non-budgetary policies results because the costs of these policies are very difficult to measure in any concrete form. More particularly, these costs do not have to pass the scrutiny of a parliament on an annual basis in the same way as budgetary policies do. Contrary to some popular opinion, there is nothing to suggest that non-budgetary policies achieve their objectives more efficiently than do budgetary policies.

One further connection between budgetary and non-budgetary policies should be noted. Each type of policy, when used to promote one policy objective, may produce side-effects that create a need for the other types of policy. For example, a non-budgetary policy such as rent regulation, may reduce rent gouging. However, a form of rent regulation which substantially reduces rents from what they would have been without regulation may be expected to discourage the supply of new rental accommodation, with consequent costs to those participating in the rental market. As a result, politicians may be put under pressure to offset the lack of new supply by initiating and expanding budgetary programs that either induce additional supply from private suppliers or replace private supply through sources of public supply. In either case, the consequence of non-budgetary policies may lead to the expanded scope of budgetary policies, with direct costs to government.

3.0 The Performance of Complementary Policies

Housing allowances, in one form or another, have gained the endorsement of many groups such as the Ontario Economic Council, the Canadian Council on Social Development and the Canadian Home Builders' Association. The appeal of housing allowances is understandable on the basis of the analysis of complementary policies on a goal by goal basis.

Much emphasis had been placed on adequacy of income (one dimension of affordable housing), as an objective of housing policy in recent years. From this perspective, a housing allowance based on prevailing rental levels appears to be clearly superior to other policies. Horizontal equity can be assured because households in comparable circumstances, even when account is taken of differential housing costs, can be treated equally. Similarly, a degree of progressivity can be built into a housing allowance to reflect concerns about vertical equity. In effect, unconstrained housing allowances can deliver assistance to a defined target group without much spill-over beyond the target group. The only likely sources of spill-over would be through changes in income between review periods or through misrepresentation of income by beneficiaries.

Housing allowances can achieve these effects with respect to adequacy of income without undue side effects in other areas. The evidence suggests that unconstrained housing allowances would not put any significant upward pressure on market rents. Moreover, these housing allowances are fully compatible with economic efficiency. Households are encouraged to balance their housing needs with other types of spending. In addition, the incentive remains to seek out the best employment opportunities regardless of location without fear of jeopardizing access to subsidized housing by having to change location.

Other programs may also offer some of the advantages of unconstrained housing allowances with respect to adequacy of income. In theory, both public housing and directed subsidies can be implemented so as to confine assistance to the target group. Unfortunately, however, experience with both these programs shows that receipt of assistance is a "hit or miss" proposition for members of the target group. In other words, these programs do well with respect to vertical equity, but perform poorly in terms of horizontal equity. They direct substantial assistance to a few in the target group but nothing to others. These programs also suffer by tying benefits to the occupancy of specified units. Households will not value the benefits as highly as equal expenditure on programs that give them the benefit of choice. The tying of benefits to specified units also creates disincentives for the efficient use of housing and for the mobility of labour.

The other dimension of affordable housing is adequacy of housing. From this perspective, a constrained housing allowance appears to be superior to other policies. Such an allowance creates strong incentives for many target households to increase their expenditures on housing. This incentive arises at the expense of both vertical and horizontal equity. Some higher income households would be assisted to a greater extent than lower income households because they are willing to spend more on housing. Similarly, not all households of similar income will be treated alike.

Constrained housing allowances are likely to be more successful than either direct subsidies or public housing in increasing the supply of rental housing. Housing allowances work by increasing the demand for housing whereas the other policies work through replacing or augmenting supply. The net addition to rental housing from these sources will be less than the housing built under the demand program because of the displacement effect earlier described. Under the most likely conditions in rental markets, this displacement effect will be substantial. Each of these alternatives to constrained housing allowances suffer the additional disadvantages, also discussed above,that they do not offer a free choice of housing and they interfere with economic efficiency.

Some of the policies considered in this study offer a measure of protection against rent gouging by raising household income, whereas others provide protection by offering alternative sources of housing. However, none of these policies can be effective in preventing rent gouging, if this is perceived to be a problem. Their failure to do so is fully understandable, and is inherent in their design. Most such policies provide assistance to households or incentives to landlords and developers on a broad basis. The exception is the directed subsidy which requires landlords to meet certain conditions for inclusion in the program. Overall, however, these programs do not provide for direct intervention into the terms of the relationship between tenant and landlord and, as a consequence, could not deal with possible instances where landlords might take advantage of vulnerable tenants, such as the elderly and single parents, to charge above market rents.

Finally, the programs differ substantially in the degree to which they affect security of tenure. Any program, to the extent it improves adequacy of income, whether by increasing household income or by decreasing effective rent, helps to overcome economic obstacles to secure tenure. Beyond this similarity, however, the policies differ in detail. Some policies, such as the various forms of housing allowances, enhance security of tenure regardless of the recipient's choice of housing. Others, particularly public housing and directed subsidies, require households to occupy designated housing in order to gain the benefit of enhanced security. As noted in the analysis, this requirement poses a dilemma for any household which has some expectation that it will not always qualify for assistance in the future. At that time, it may be forced to seek other accommodation.

4.0 The Performance of Rent Control

The housing programs reviewed in this study are complementary to rent controls in the sense that they can be used in combination with rent controls to achieve the objectives of housing policy. However, there is not a single method through which complementary policies may be most effectively combined with rent regulation. Since these policies can be combined in a multitude of ways, the choice of the appropriate combination becomes especially important, particularly in terms of effectiveness for cost.

Rent controls were not themselves subjected to the same assessment in this study as were the complementary policies yet enough evidence exists from other sources to make at least a preliminary assessment of the strengths and weaknesses of controls in achieving particular objectives relative to the complementary policies assessed in this study. Stanbury (1984a) and Stanbury and Vertinsky (1985) have presented extensive material on the ability of rent controls to achieve their stated objectives. Their analysis suggests that the weaknesses of rent controls correspond to the strengths of the complementary policies and, to a degree, vice-versa.

Complementary policies, in particular housing allowances, are capable of achieving the adequacy of income objective effectively by directing assistance to target households. In contrast, rent controls only do so in a haphazard way. Benefits accrue to households well beyond the target group, sometimes by a substantial margin. Moreover, rent controls do not provide benefits uniformly, or even at all, to all members of the target group. Stanbury and Vertinsky (1985) conclude as follows:

> i) For tenants living in rent controlled units 83.5% of the total benefits went to the 56% of tenant households with an annual income above $15,000 in 1981. The 44% of tenants with incomes under $15,000 received only 16.5% of the total benefits. The 24% of tenants with a household income above $25,000 received 38.4% of the total pecuniary benefits -- an average of $432 per household per year. In contrast, households below $15,000 receive only about $102 per year in benefits in the form of rent below the equilibrium level.
>
> ...
>
> iii) While tenants in the controlled sector received some $228 million in rent control benefits, those in the uncontrolled sector (but not living in social housing) paid some $34 million in higher rents because of rent control. Some 77% of the total higher rent payments were made by the 72% of households in the uncontrolled sector with incomes above $20,000 in 1981.
>
> iv) While households with an income below $20,000 (recall the average in 1981 was $17,600) in the controlled sector received some $91 million in pecuniary benefits, those in the uncontrolled sector paid higher rents amounting to about $8 million in 1981. (6-112)

They amplify their observations with respect to those households harmed by rent regulation:

> ...we have cited some studies...which suggest that the main beneficiaries of rent controls were renters who would be able to enjoy affordable housing in any case. Indeed, some of the "costs" of controls were incurred by new entrants to the rental housing markets (often young singles with lower incomes or elderly moving from the homeownership sector) who had to find housing in the uncontrolled sector. The "mobile", "uninformed" and the new entrants have been more vulnerable to "black markets" and find it more difficult in some cases to utilize the regulatory machinery because of high transaction costs. (7-13)

Stanbury and Vertinsky (1985) suggest a better performance of rent controls with respect to other objectives:

> On balance, it appears that Ontario's rent controls have largely achieved objectives 1 [rent gouging] and 5 [stabilizing the path of adjustment]... (7-16)

With respect to the objective of rent gouging, they state:

> Our analysis indicates that the system has generally prevented "gouging" (Objective 1), although as Stanbury...points out, the term has several meanings. (7-10)

The latter objective, for which Stanbury and Vertinsky (1985) identified success for rent controls -- stabilizing the path of adjustment -- was not considered for complementary policies in this study. The main reason for this omission was that this objective was a short-run policy objective, whereas complementary policies appear best suited for dealing with longer run problems in the rental housing market.

Any benefits perceived from rent controls cannot be derived without costs elsewhere. In particular, the benefits from rent controls must be balanced with its costs with respect to adequacy of housing. Stanbury and Vertinsky (1985) suggest that:

> Rent regulation has done little to assure that there is an adequate supply of "decent, affordable" rental housing for those with low to moderate income (Objective 4). Since rent controls have been in effect in Ontario, the supply of new rental units has decreased, as the following data on average annual rental starts indicates

1969-1974	37,641 units
1975-1979	14,259 units
1980-1984	14,491 units

> ...We note that new rental starts fell at a time that vacancy rates were also falling. (7-14)

Stanbury and Vertinsky (1985) do not attribute this decline in rental starts solely or even primarily to rent controls. They state:

> While controls have definitely pushed up the costs and the risks associated with supplying new rental units, the significant decline in new construction of rental units since controls were introduced cannot be attributed only or even mainly to their introduction. In our opinion the demographic shift (i.e., a significantly lower level of increase in population) was the major factor to which supply of new rental housing responded. (7-15)

This view can be contrasted with that of Smith and Tomlinson who argue:

> Rent control has substantially depressed new rental housing starts in Ontario even though newly constructed dwellings are exempt from the controls. The steady decline in the real cash flow and real capital value of existing rental dwellings under rent control greatly reduces the desirability of investing in new rental housing by changing the investment climate and creating fears that controls would eventually be extended with the same consequences to newly constructed projects. (1981, p. 97)

The demographic factors cited by Stanbury and Vertinsky (1985) are not in themselves enough to account for the change in starts. They state:

> ...while annual average rental starts were falling by 62% between 1969-74 and 1978-79, new household formation was falling by 18% between 1971-76 and 1976-81. Although average annual household formation continued to fall (by 28% between 1976-81 and 1981-86e), annual average rental starts were the same between 1975-79 and 1980-84. (6-75)

Stanbury and Vertinsky also raise the possibility of other causal factors, such as increased nominal and real interest rates, higher unemployment rates, growth of per capital income, the misclassification of condominiums built for rental purposes, income tax changes and revisions to the Landlord and Tenant Act in 1970 and 1975.(1) Clearly, the effect of rent controls on the supply of rental housing is very difficult to disentangle from other forces that influence rental starts. However, a clearer picture of the effect of rent controls on the private supply of rental housing can be gained from examining the changing composition of rental starts. Evidence which Stanbury and Vertinsky (1985) present from Smith and Tomlinson (1981) are shown in Table 8.1. It appears that rent controls have been a substantial influence, among other factors, on the private supply of rental units. This supports the earlier observation that non-budgetary policies may through their side-effects induce pressures for increased budgetary programs. This phenomenon has very important direct cost consequences for government, particularly provincial governments at this time.

5.0 The Choice of Policy in Perspective

The minimization of the costs to society of achieving policy goals is an important guiding principle for governments at any time. At present, however, there are additional factors which make this principle especially important for the formulation of housing policy in Ontario. First, the provincial government has announced the extension of rent controls coverage to include nearly all rental units, regardless of date of construction or level of rent. Second, the federal government appears to be on the verge of changing

TABLE 8.1

Composition of Rental Housing Starts

	Private unsubsidized starts	Government-assisted starts
1969-74	27,250	8,717
1975-80	6,240	8,535

SOURCE: Smith and Tomlinson (1981) from Stanbury and Vertinsky (1985) p. 6-80.

its approach to housing policy by transferring responsibility for social housing programs to provincial control (see Ch. 3, pp. 176-77). These developments underline the urgency of developing the best choice of policies. The first factor, the extension of rent controls, means that their undesirable effects, whatever their present extent, will be exacerbated. In particular, side-effects which previously have led to increased governmental responsibility for public housing are likely to be increased. The second factor, changing federal policies, increases the significance of the first. The increased demand for public finance of rental housing is likely to bring increased pressure on the provincial government at the very time when the federal government is seeking to reduce or prevent the extension of its own commitments to further expenditures. The combined effect of these two developments makes the choice of an appropriate mix of complementary policies even more difficult and important than it has been in the past.

Note to Chapter 8

(1) Under cross-examination during the June 24th, 1985 hearing of the Commission of Inquiry into Residential Tenancies, Stanbury indicated that the demographic shift was not the major factor as indicated above. Rather the combined impact of these various factors was likely responsible (See, also Stanbury and Vertinsky, 1985, pp. 6-82 to 6-83).

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Research Studies

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1 Slack, Enid and Sherry Glied. Rent Registry Alternatives.

2 Reid, Frank. Collective Bargaining for Tenants.

3 Jaffary, Karl D. Problems in the Regulation of Rents for Roomers and Boarders.

4 MacDonald, Daniel V. Constitutional Reference Re: The Residential Tenancies Act.

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7 Sharp, Campbell, Pannell Kerr Forster Campbell Sharp. Survey of Financial Performance of Landlords.

8 Marks, Denton. Housing Affordability and Rent Regulation.

9 Steele, Marion and John Miron. Rent Regulation, Housing Affordability Problems, and Market Imperfections.

10 Clayton Research Associates Limited. Rent Regulation and Rental Market Problems.

11 Makuch, Stanley M. and Arnold Weinrib. Security of Tenure.

12 Hartle, D.G. The Political Economy of Residential Rent Control in Ontario.

13 Slack, Enid and David P. Amborski. The Distributive Impact of Rent Regulation.

14 Knetsch, Jack L., Daniel Kahneman and Patricia McNeill. Residential Tenancies: Losses, Fairness and Regulations.

15 Stanbury, W.T. Normative Bases of Rent Regulation.

16 Stanbury, W.T. Normative Bases of Government Action.

17 Stanbury, W.T. and P. Thain. The Origins of Rent Regulation in Ontario.

18 Stanbury, W.T. and I.B. Vertinsky. Rent Regulation: Design Characteristics and Effects.

19 Chant, John. Overview of Alternative Rental Housing Policies.

20 Foot, David K. Housing Demands: A Demographic Perspective.

21 Quirin, G. David. Regulatory Systems and their Applicability to Rent Controls.

22 Mascall, M. and Associates. Report of the Ontario Rental Housing Market.

23 Environics Research Group Limited. Financing Residential Rental Accommodation: A Survey.

24 Ekos Research Associates Inc. A Study of Landlords and Rent Regulation.

25 des Rosiers, Francois. A Rent Control System in Quebec.

26 Slack, Enid. The Costs of Rent Review in Ontario.

27 Muller, Andrew. Workable Rent Regulation: A Synthesis.

The following is a list of papers prepared by the research staff of the Inquiry.

28 Adams, Eric B., Pearl Ing and John Pringle. A Review of the Literature Relevant to Rent Regulation.

29 Adams, Eric B., Pearl Ing, Janet Ortved and Mary Jane Park. Government Intervention in Housing Markets: An Overview.

30 Pringle, John. Ontario's Residential Tenancies: A Statistical Profile.